For discussion
on 7 July 2014

Legislative Council
Panel on Financial Affairs

Consultation Conclusions on Corporate Insolvency Law Improvement Exercise and Detailed proposals on a new Statutory Corporate Rescue Procedure

PURPOSE

This paper briefs Members on the outcome of the public consultation on the corporate insolvency law improvement exercise and the Administration responses, and the detailed proposals on a new statutory corporate rescue procedure ("CRP") and insolvent trading provisions.

Part I - CORPORATE INSOLVENCY LAW IMPROVEMENT EXERCISE

Background

2. We received a total of 36 written submissions during the public consultation exercise on legislative proposals to improve the corporate insolvency and winding-up provisions in the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32) ("C(WUMP)O"), which ended on 15 July 2013. The objectives of the proposals are to facilitate more efficient administration of the winding-up process and increase protection of creditors through streamlining and rationalising the company winding-up process having regard to international experience. A compendium of the submissions is available on the Financial Services and the Treasury Bureau's website[1].

Outcome of Consultation

3. All 46 legislative proposals set out in the consultation document were supported by a majority of respondents. The consultation conclusions with a summary of the comments made by respondents and the Administration's responses are at **Annex A**.

4. In response to the comments raised by respondents, we would refine the proposals in the following areas –

(a) in response to requests to clarify the nature of the various types of

[1] The website is http://www.fstb.gov.hk/fsb.

provisional liquidators appointed under section 194 of the C(WUMP)O in a court winding-up[2], we will introduce specific provisions to clarify the powers, duties, remuneration, etc. of these different types of provisional liquidators, instead of designating all such provisional liquidators as liquidators as originally proposed (paragraphs 3.32 to 3.33 of the consultation document refer);

(b) having regard to the fact that a receiver or a receiver and manager would usually be appointed by a secured creditor and is mainly accountable to the latter, we agree to the comments received that the question of whether a person is appropriate to take up the role of receiver or receiver and manager should rest with the secured creditor concerned, and hence the proposals on the disqualification of certain categories of persons who are considered as having a conflict of interest for appointment as a liquidator or a provisional liquidator should not apply to the appointment of a receiver or a receiver and manager of the property of a company (paragraphs 3.13 to 3.18 of the consultation document refer);

(c) to enhance the integrity of the appointment process of a provisional liquidator or liquidator, we agree that in addition to the requirement for a prospective provisional liquidator or liquidator to disclose the facts or relationships in a statement of relevant relationships (paragraph 3.21 of the consultation document refers), such person should be required to state whether his immediate family member has, at any time within the immediately preceding period of two years, been a receiver or receiver and manager of the company's property. This is in response to comments that a receiver or a receiver and manager of a company is directly involved in and is familiar with the operation and business of the company, and therefore it is necessary for the prospective provisional liquidator or liquidator to make a disclosure if his immediate family member has taken up such a role in respect of the company concerned; and

(d) we will refine the definition of "associate" for the proposed provisions on voidable transactions (paragraph 5.20(e) of the consultation document refers) to the effect that a person would be considered as having control of a company if he is entitled to exercise, or control the exercise of, more than 30% of the voting power (instead of one third or more as originally proposed) at any general meeting of the

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[2] Under section 194 of C(WUMP)O, the following office-holders who take office upon and after the making of a winding-up order are all called the "provisional liquidator"–

(a) except where a person other than the Official Receiver acts as a provisional liquidator under section 194(1)(aa), the Official Receiver by virtue of his office becomes the provisional liquidator under section 194(1)(a) upon the making of the winding-up order;

(b) where a person other than the Official Receiver has been appointed as a provisional liquidator by the court under section 193 of the C(WUMP)O before the making of the winding-up order, this person continues to act as the provisional liquidator by virtue of section 194(1)(aa); and

(c) the Official Receiver as the provisional liquidator under (a) may appoint one or more persons as provisional liquidator under section 194(1A) in place of himself.

company or of another company which has control of it, so as to align the threshold of "control" in the said definition with relevant provisions in the new Companies Ordinance (Chapter 622) ("the CO") and the Listing Rules.

Next Steps

5. Backed by the overwhelming support for this legislative exercise, we will proceed to prepare the amendment bill with a view to introducing it into the Legislative Council in 2015. We will continue to engage relevant stakeholders as we prepare the amendment bill.

Part II - STATUTORY CORPORATE RESCUE PROCEDURE AND INSOLVENT TRADING PROVISIONS

Background

6. As reported to the Panel in January 2014[3], we have been actively developing further the proposals to introduce a new statutory CRP and the insolvent trading provisions, having regard to the outcome of the public consultation exercise in 2009-10 on the conceptual framework and some specific issues ("the 2009-10 consultation exercise"). In particular, we have also considered in detail various other key issues which were not discussed in the previous consultation.

Detailed Proposals on a statutory CRP and Insolvent Trading provisions

7. We have prepared a package of detailed proposals on the statutory CRP and the insolvent trading provisions which are set out in **Annex B** and **Annex C** respectively. An overview of the key features of the proposals is set out in paragraphs 8 to 37.

(1) Statutory Corporate Rescue Procedure

8. At present, a company in financial difficulties may opt to pursue to come to an "arrangement or compromise" with its creditors under section 673 of the CO. However, an "arrangement or compromise" does not provide for a statutory moratorium on legal actions which can bind creditors to facilitate the formation of a rescue plan. Besides, an "arrangement or compromise" also requires considerable court procedures which could be costly and time-consuming.

9. The aim of a statutory CRP is to provide an option for companies in short-term financial difficulties to initiate the procedure with a view to turning around and reviving its business as much as possible, instead of pursuing liquidation immediately to wind up the company. We have taken into account

[3] See the Panel paper CB(1)625/13-14(08).

the following key considerations in designing the CRP–

(a) the CRP should stipulate a defined timeframe for specified actions to facilitate speedy determination by creditors on the way forward for the company;

(b) there would be provisions for the appointment of an independent third party, namely the provisional supervisor ("PS"), to take temporary control of the company, consider options for rescuing the company and prepare proposals for a voluntary arrangement ("VA");

(c) the PS would be required to make recommendations on the specified alternative outcomes (see paragraph 25) for the creditors' consideration and decision;

(d) to enable the PS to focus on the formulation of the rescue plan, there should be a moratorium on legal actions and proceedings against the company when the company is under provisional supervision;

(e) there should be appropriate checks-and-balances measures on the exercise of powers by the PS[4];

(f) employees of the company should be no worse off than in the case of an immediate insolvent winding-up; and

(g) the CRP should involve predominantly out-of-court arrangements to save time and costs.

Statutory objective of a CRP

10. It is important that the PS should work towards a clear objective. We propose that the statutory objective of CRP should be specified as maximising the chance of existence of the company or as much as possible its business, and if this is not attainable, achieving a better return for the creditors of the company than in case of an immediate insolvent winding-up.

Initiation of the CRP

11. We propose that the CRP may be initiated by the company (either by resolution of its members or directors) or, where the company has already entered into winding-up process, by the provisional liquidator or liquidator (as the case may be) through the appointment of a PS if they are of the opinion that the company is insolvent or likely to become insolvent[5].

[4] If a resolution is passed to approve the proposed VA at the final creditors' meeting, the PS would become the supervisor of the VA. The supervisor would oversee the implementation of the VA - see paragraph 28. The checks-and-balances on the exercise of powers by the PS would similarly apply to the exercise of powers of the supervisor during the implementation of the VA.

[5] The existing insolvency test used in section 178 of the C(WUMP)O would be adopted (i.e. a mixture of the cashflow and balance sheet tests).

12. Having regard to prevailing international practices that the major secured creditor of a company is allowed to play a significant role in the process for initiating the CRP, and since the rights of secured creditors to enforce their securities are stayed under the moratorium during the CRP process, we propose that a company seeking to commence the CRP process by appointment of a PS should be required to obtain the prior written consent of its major secured creditor. In response to stakeholders' comments, we will consider further whether, in case the company does not have a major secured creditor, consent from all secured creditors would be required before the company could initiate the CRP.

Appointment of PS

13. In accordance with the conclusions of the 2009-10 consultation exercise, we propose that certified public accountants and solicitors with practicing certificates would be qualified to be appointed as a PS so as to allow greater market flexibility in this new area of practice. In the event that there are complaints against the PS's conduct in relation to the CRP, such complaints would be addressed to the Hong Kong Institute of Certified Public Accountants ("HKICPA") or the Law Society of Hong Kong for disciplinary action as appropriate.

14. We propose that certain categories of individuals, e.g. those who are considered to have conflict of interest, would be disqualified from acting as a PS. This is in line with a similar proposal under the corporate insolvency law improvement exercise which applies to the appointment of provisional liquidators and liquidators (paragraph 4(b) refers). Also, we propose that prospective PSs should also be required to prepare a declaration of relevant relationship (modelling on a similar proposal under the corporate insolvency law improvement exercise which applies to provisional liquidators and liquidators (paragraph 4(c) refers)) and a declaration of indemnity to enable the creditors to make an informed decision at the first creditors' meeting on whether his appointment is appropriate (see paragraph 16 on the first creditors' meeting).

Duties and powers of PS and checks-and-balances measures

15. During the period of provisional supervision, the PS would become an agent of the company and would assume control of the company's business, affairs and property. The functions and powers of the officers of the company would be suspended, except to the extent as approved by the PS.

16. The PS would be required to call the first creditors' meeting, to be held within 10 business days from the commencement of provisional supervision, for considering whether to maintain or replace the PS appointed by

the initiating party and whether to appoint a committee of creditors[6] (and if so, its membership). The PS would also be required to call the final creditors' meeting, to be held within 45 business days from the commencement of provisional supervision, for making a decision on the future of the company by voting on the specified alternative outcomes for the company. For the purpose of facilitating creditors' decision on these questions, the PS is responsible for providing his opinion on each of the three alternative outcomes. Besides, he would also submit investigation reports covering the company's business, property affairs and financial circumstances to creditors to facilitate their deliberation at the final creditors' meeting.

17. To enable the PS to discharge his duties effectively, he would be empowered to, inter alia, –

(a) remove a director of the company, and appoint replacement or additional directors;

(b) request certain categories of persons to give a statement of affairs[7] or deliver the books and papers of the company to him (in the case of directors and the secretary of the company, they would be required by law to provide a statement of affairs to the PS upon request within a specified period); and

(c) apply to the court for examination of any officer of the company or any other person[8] on specified ground.

18. In order for a CRP to be successful, it is important to maintain the confidence of others trading with the company. The PS should also be encouraged to perform due diligence prior to accepting the appointment, and to exercise prudence during provisional supervision. With these considerations, we propose that the PS would be subject to personal liability in respect of two categories of contracts, as follows –

(a) pre-appointment contracts which are positively adopted by him. In this regard, the PS would be given a period of 16 business days from commencement of provisional supervision for deciding whether to adopt any pre-appointment contracts[9], including employment contracts; and

(b) new contracts entered into by him as the PS.

The PS would be allowed to agree with the concerned contracting parties on

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[6] The functions of the committee of creditors are to be consulted any matters relating to the provisional supervision; and to receive and consider reports by PS on the business of the provisional supervision.

[7] The statement of affairs should show the particulars of the company's assets, debts, and liabilities, the particulars of its creditors, the details of the securities held by the creditors, and any further information as required by the PS.

[8] Other person refers to any person known or suspected by the PS to have in his possession any property of the company or indebted to the company; or any person that the court thinks capable of giving information concerning the promotion, dealings, affairs etc. of the company.

[9] Contracts would not be deemed to be adopted by the PS if he has not adopted them.

the extent of his personal liability in respect of the relevant contracts. In addition, the PS would be entitled to be indemnified out of the company's property in his custody for debts he is personally liable in his capacity as the PS, and the indemnity would have priority over all other claims e.g. floating chargees and unsecured creditors.

19. As a checks-and-balances measure, we propose that the court may, on application by an eligible party[10], examine the conduct of the PS[11] for misfeasance or breach of duty and, where appropriate, make an order against him (e.g. to order payment of compensation to the company). In addition, to provide proper safeguards to creditors' and members' interests, we propose that any creditor or member of the company may apply to the court against the PS on specified ground (e.g. the PS having done an act that is or would be prejudicial to the interests of some or all of the company's creditors or members). In such case, the court may make such order as it thinks fit.

Treatment of employees' outstanding entitlements

20. Based on the conclusions of the 2009-10 consultation exercise which represent the outcome of discussions with different stakeholders, there would be a phased payment schedule for outstanding employees' entitlements as at the commencement of the CRP owed by the company. Specifically, to ensure that employees would be no worse off than in the situation when the company goes into immediate insolvent winding-up –

(a) arrears of wages before the commencement of provisional supervision should be paid up to the cap of the Protection of Wages on Insolvency Fund ("PWIF") by the 30th calendar day after the commencement of provisional supervision;

(b) for employees whose employment had been terminated before the commencement of provisional supervision, payments up to the relevant PWIF-caps for any outstanding wages in lieu of notice of termination, severance payments, pay for untaken annual leave and pay for untaken statutory holidays (i) within 45 calendar days after the VA has been approved; or (ii) if the time limit for holding the final creditors' meeting is extended (see paragraph 26), within 45 calendar days from the date of the approval of the extension; and

(c) any remaining pre-commencement entitlements, including outstanding employers' contributions under the Mandatory Provident Fund Schemes Ordinance (Chapter 485) or the Occupational Retirement Schemes Ordinance (Chapter 426), should be paid in full within 12 months after the VA has come into effect.

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[10] The Official Receiver, the incumbent PS (to take action against a former PS), the liquidator, any creditor or member of the company may make such application.

[11] Within the meaning of this paragraph, PS means an incumbent PS or a former PS.

Moratorium and its exemptions

21. There would be a moratorium on legal actions and proceedings against the company (e.g. a winding-up petition against the company) and that all such actions and proceedings would be stayed during the period of provisional supervision, save with the leave of court or the PS's consent (as the case may be).

22. There would be certain exemptions from the moratorium. In line with the conclusions of the 2009-10 consultation exercise, employees whose payments as mentioned in paragraph 20 are not fulfilled and employees whose entitlements arising after the commencement of CRP are in arrears would not be bound by the moratorium and may file winding-up petition against the company. Besides, petitions made under sections 723 to 727 of the CO, which provide for applications to the court for appropriate remedies in case a company's affairs are conducted in a manner unfairly prejudicial to the interests of minority shareholders, would also be exempt.

23. In line with the conclusions of the 2009-10 consultation exercise, the moratorium would not prohibit set-off against the company, i.e. the parties can net their obligations when the moratorium comes into operation. This will also ensure a more equitable share of creditors' voting rights.

24. The moratorium would also allow the enforcement of contractual terms which provide for the termination of contract upon specific events such as the insolvency of the company or the commencement of its provisional supervision (i.e. *ipso facto* contractual clauses). Since both setting-off and the enforcement of ipso facto clauses would be allowed during the moratorium, it obviates the need to consider whether there should be specific exemption for some financial contracts and what sort of financial contracts should be exempted from the moratorium.

End or extension of provisional supervision – specified alternative outcomes

25. We propose that the final creditors' meeting to be held within 45 business days after the commencement of the provisional supervision would decide whether –

(a) the proposed VA should be approved with or without modification; or

(b) the company should be wound up; or

(c) the provisional supervision should end, for the company to revert to its pre-CRP status.

26. The time limit for holding the final creditors' meeting may be extended –

(a) by approval of the creditors at a creditors' meeting, provided that the extended period is within six months from the commencement of the provisional supervision; or

(b) by order of the court on application made by the PS at any time for such period as the court thinks fit.

27. It does not accord with the policy objective of the CRP to allow provisional supervision to carry on indefinitely. Therefore, under the proposals, provisional supervision would end in the following circumstances –

(a) upon passage of any one of the three specified outcomes set out in paragraph 25 above; or

(b) in other specified circumstances, such as –

(i) in accordance with an order by the court;

(ii) where the final creditors' meeting is not held within 45 business days or such extended period as determined under paragraph 26; or

(iii) where the final creditors' meeting does not approve any of the specified outcomes set out in paragraph 25 above.

VA

28. If a resolution to approve the proposed VA is passed at the final creditors' meeting, the PS would become the supervisor of the VA (unless the creditors appoint another person to be the supervisor), who would oversee the implementation of the VA. There would be statutory duties for the supervisor in respect of keeping accounts and records and making regular reports to the company and creditors, filing notices, etc. Other duties and powers of the supervisor would be as set out in the VA. The qualification requirements for and the disciplinary regime of supervisor would be the same as those for a PS.

29. The VA would bind the company, its officers and members, the supervisor and all relevant creditors (including employees with pre-commencement outstanding entitlements). There would be a moratorium on legal proceedings and actions by persons bound by the VA.

Offence provisions

30. To ensure the integrity of the CRP, there would be offence provisions to address situations where relevant persons have failed to comply with certain statutory requirements. These include offences for –

(a) a PS or a supervisor who has not complied with the relevant statutory requirements, e.g. in the case of a PS, the duty to call the first and the

final creditors' meetings, and the filing, notification and publicity requirements, etc.;

(b) an unqualified/disqualified person who acts as a PS or a supervisor;

(c) a director or secretary of the company who does not comply with the requirement to provide a statement of affairs to the PS within the specified period; and

(d) a person who has not complied with the PS's request for a statement of affairs or the books and papers of the company.

Applicability of CRP

31. The option of CRP would be open to all companies registered under the CO[12], except for those which are authorised institutions regulated by the Hong Kong Monetary Authority, authorised insurers regulated by Office of the Commissioner of Insurance and licensed corporations or relevant entities regulated by Securities and Futures Commission, since they are subject to statutory regulatory regimes under which the relevant regulators have statutory power to assume control over them or oblige them to act in a certain manner.

32. To facilitate Members' understanding of the procedural flow of a typical CRP case, a flowchart is attached in **Annex D.**

(2) Insolvent trading provisions

33. It is important that directors of companies in financial difficulty should act on insolvency earlier rather than later. Besides, there is a need to protect the interests of creditors dealing with a company which is getting into financial difficulty. Therefore, we propose that after a company goes into liquidation, the liquidator of the company should be empowered, under specified circumstances, to make an application to the court to seek a declaration that a director[13] of the company is civilly liable for insolvent trading and to make an order for the director to pay compensation to the company which traded while insolvent. There will be defence provisions for directors.

Constituents of liability and statutory defence

34. Taking into account the comments received during the 2009-10 consultation exercise about the need to clarify the specific elements in establishing the liability on insolvent trading, we propose that the court must be

[12] This also includes companies registered under the former Companies Ordinances.

[13] In accordance with the conclusions of the 2009-10 consultation exercise, "senior management" would be excluded from being liable under the insolvent trading provisions. The proposed definition of "director" includes shadow directors of the company. In accordance with section 2 of the CO, a shadow director means a person in accordance with whose directions or instructions (excluding advice given in a professional capacity) the directors, or a majority of the directors, of the company are accustomed to act.

satisfied that all the following constituents of liability have been met before it makes a declaration of insolvent trading in respect of the person so liable –

(a) there is an incurrence of a debt by the company;

(b) the person concerned is a director of the company at the time the company incurs the debt;

(c) the company is insolvent at that time or becomes insolvent by incurring that debt, or debts including that debt;

(d) the director concerned failed to prevent the company from incurring the debt; and

(e) the director concerned knew or ought to have known that the company was insolvent at that time or would become insolvent by incurring that debt or debts including that debt.

In determining whether the director concerned has the constructive knowledge in sub-paragraph (e) (i.e. he "ought to have known"), the same test used in the CO regarding directors' duty of care, skill and diligence would apply.

35. We propose that it would be a statutory defence if –

(a) the director has taken all reasonable steps to prevent the company from incurring the debt; or

(b) the incurring of the debt is part and parcel of the steps taken by the director concerned to initiate the CRP process.

36. As regards (b), we will consider further the comments we received from some stakeholders that since CRP is intended to be an additional option for companies in financial difficulties to pursue, whether the scope of the proposed defence should be expanded to cover also an "arrangement or compromise" or an informal workout.

37. Compensation obtained from directors would be paid to the company, which would increase the assets of the company available for distribution to the unsecured creditors in a winding-up.

Feedback of Stakeholders' Engagement

38. We have conducted discussion sessions with the HKICPA, the Hong Kong Association of Banks, the Law Society of Hong Kong, the Hong Kong Institute of Directors and chambers of commerce to discuss the detailed proposals on the CRP and the insolvent trading provisions. We have also consulted the relevant Advisory Group[14] on these detailed proposals. They

[14] The Advisory Group was established in 2012 to provide technical inputs and expert advice to the Government on the corporate insolvency law improvement exercise. It is chaired by the Official Receiver and comprises representatives from the professional bodies, practitioners, the academic sector and individual members of the Standing Committee on Company Law Reform.

indicated general support for the legislative exercise, and also provided detailed comments on individual aspects of the proposals.

Next Steps

39. We will study the detailed comments from stakeholders carefully and will continue to engage them as we prepare the necessary legislation. Having regard to the scale of the exercise and the complexity of the issues involved, our target is to complete the drafting of the amendment bill within the current term of the Legislative Council.

40. Members are invited to –

(a) note the consultation conclusions on the corporate insolvency law improvement exercise; and

(b) give their views on the detailed proposals on the introduction of a statutory CRP and insolvent trading provisions as set out in paragraphs 8 to 37.

Financial Services and the Treasury Bureau
28 May 2014

Improvement of Corporate Insolvency Law Legislative Proposals

Consultation Conclusions

BACKGROUND

On 16 April 2013, the Financial Services and the Treasury Bureau ("FSTB") launched a three-month public consultation to solicit views on 46 legislative proposals to improve the corporate insolvency and winding-up provisions in the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32) ("C(WUMP)O"). The objectives of the proposals are to facilitate more efficient administration of the winding-up process and increase protection of creditors through streamlining and rationalising the company winding-up process having regard to international experience.

2. The consultation document[1] was issued to various stakeholders, including relevant professional bodies, market practitioners, chambers of commerce, financial regulators, etc. It was also posted on the websites of FSTB and the Official Receiver's Office ("ORO"). Hard copies were made available to the general public at a number of Government offices. Besides, FSTB and ORO briefed the Panel on Financial Affairs of the Legislative Council ("LegCo") and the Standing Committee on Company Law Reform on the legislative proposals on 3 May 2013 and 25 May 2013 respectively, and held a public consultation forum on 22 May 2013. We also attended nine seminars and meetings convened by other interested organisations to brief the participants on the proposals and to listen to their views (details of these seminars and meetings are at **Appendix I**).

CONSULTATION FEEDBACK

3. We received a total of 36 written submissions during the consultation, which ended on 15 July 2013. Out of these submissions, 17 were from business and professional organisations, ten from professional service providers, three from individuals, three from political/labour organisations, two from statutory organisations and one other respondent who requested not to disclose his identity. A list of the respondents is at **Appendix II**. A compendium of the submissions will be made available on FSTB's website.

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[1] The consultation document is available at http://www.fstb.gov.hk/fsb/ppr/consult/doc/impcill_consult_e.pdf.

4. All 46 legislative proposals set out in the consultation document were supported by the majority of respondents. Respondents have also made specific comments on some of the proposals, and our responses to these specific comments are set out in **Appendix III**. In particular, we have reviewed and refined some of the original proposals in light of these comments. For easy reference, we have highlighted these modifications in paragraphs 5 to 8 below. As regards other proposals which received different views from some respondents, we do no propose any change to these proposals and have explained our considerations in paragraphs 9 to 29 below.

Proposal to clarify the nature of "provisional liquidators" in a court winding-up

5. To clarify the nature of all types of "provisional liquidators" in a court winding-up, we have proposed to –

(a) designate all provisional liquidators who take office upon and after the making of a winding-up order under different sub-sections of section 194 of C(WUMP)O (collectively referred to herein as "section 194 PL")[2] as "liquidators" so that they will be subject to the provisions in the C(WUMP)O which apply to liquidators (such as provisions relating to powers, duties, remuneration, etc.) *(Question 12)*; and

(b) provide more clearly that it is up to the court, taking into account case-specific circumstances, to determine the powers, duties, remuneration and termination of appointment of a provisional liquidators appointed by the court before the making of a winding-up order under section 193 of C(WUMP)O ("section 193 PL") *(Question 13)*.

6. Respondents generally agreed that it was necessary to provide more clarity in certain existing provisions of C(WUMP)O that make reference to provisional liquidators on which type of provisional liquidator is being referred to. However, while the vast majority of respondents expressed support for proposal (b), some respondents were concerned that proposal (a) would

[2] Under section 194 of C(WUMP)O, the following office-holders who take office upon and after the making of a winding-up order are all called the "provisional liquidator"–
(a) except where a person other than the Official Receiver acts as a provisional liquidator under section 194(1)(aa), the Official Receiver by virtue of his office becomes the provisional liquidator under section 194(1)(a) upon the making of the winding-up order;
(b) where a person other than the Official Receiver has been appointed as a provisional liquidator by the court under section 193 of the C(WUMP)O before the making of the winding-up order, this person continues to act as the provisional liquidator by virtue of section 194(1)(aa); and
(c) the Official Receiver as the provisional liquidator under (a) may appoint one or more persons as provisional liquidator under section 194(1A) in place of himself.

unintentionally change the powers of certain types of section 194 PLs. In particular, some respondents were concerned that creditors' interests might be undermined if a provisional liquidator appointed under section 194(1)(aa) of C(WUMP)O, who has not yet received the approval of the creditors and contributories for his appointment, is given full and unrestricted powers to carry out all the duties in the same way as liquidators by virtue of proposal (a).

7. Having regard to such concerns, we will modify proposal (a) by introducing specific provisions to clarify the powers, duties, remuneration, etc. of different types of section 194 PL. These include –

(a) providing that the powers of the provisional liquidator appointed under section 194(1)(aa) of C(WUMP)O would be restricted to those set out in section 199(4) to (6) of the C(WUMP)O[3];

(b) providing to the effect that the Official Receiver ("OR") in her capacity as a provisional liquidator appointed under section 194(1)(a) of C(WUMP)O would have the same powers as a liquidator; and

(c) making no change to the provisions governing the powers of the provisional liquidator appointed by OR under section 194(1A) of C(WUMP)O.

Other refinements to the original proposals

8. The other refinements to the legislative proposals are explained below –

(a) we will not apply the proposals on the disqualification of certain categories of persons (e.g. those who are considered as having a conflict of interest) for appointment as a provisional liquidator or a liquidator to the appointment of a receiver or a receiver and manager of the property of a company (paragraphs 3.13 to 3.18 of the consultation document refer), having regard to comments that a receiver or a receiver and manager would usually be appointed by a secured creditor and is mainly accountable to the latter and therefore, the question of whether a person is appropriate to take up the role of receiver or receiver and manager should rest with the secured creditor concerned;

(b) we will require a prospective provisional liquidator or liquidator to state whether any of his immediate family members have, at any time within

[3] These provisions currently apply to a provisional liquidator appointed by the OR under section 194(1A) in place of himself.

the immediately preceding period of two years, been a receiver or receiver and manager of the company's property, in addition to the requirement for him to disclose the facts or relationships in a statement of relevant relationships as set out in paragraph 3.21 of the consultation document. This is in response to comments that a receiver or a receiver and manager is directly involved in and is familiar with the operation and business of the company, and therefore it is necessary for the prospective provisional liquidator or liquidator to make a declaration if any of his immediate family members have taken up such a role in respect of the company; and

(c) we will amend the definition of "associate" for the proposed provisions on voidable transactions (paragraph 5.20(e) of the consultation document refers) to the effect that a person is to be considered as having control of a company if he is entitled to exercise, or control the exercise of, more than 30% of the voting power (instead of one third or more as originally proposed) at any general meeting of the company or of another company which has control of it. This is in response to suggestions that the threshold of "control" in the said definition should align with relevant provisions in the new Companies Ordinance (Chapter 622) ("new CO")[4] and the Listing Rules[5].

Proposal to introduce new provisions on "transactions at an undervalue"

9. For better protection of creditors against depletion of the assets of an insolvent company, we have proposed to introduce new provisions to empower the court to make orders in relation to a company which has entered into a transaction at an undervalue[6] before its winding-up (e.g. to invalidate the transaction). Under our proposals, the "relevant time" for a transaction at an undervalue to be caught would be any time within the period of five years ending with the commencement of the winding-up, but only if at that time the company was unable to pay its debts or became unable to pay its debts as a result of the transaction *(Question 25)*.

10. An overwhelming majority of respondents supported introducing provisions to empower the court to make orders in relation to a company which has entered into a transaction at an undervalue before its winding-up, and most of them agreed that the "relevant time" should be any time within the period of

[4] Section 488(1) of the new CO.

[5] Rule 1.01 of the Main Board Listing Rules or the GEM Listing Rules.

[6] A transaction at an undervalue occurs when a company makes a gift to or enters into a transaction with a person on terms that provide for the company to receive no consideration; or enters into a transaction with a person for a consideration (to be assessed in terms of money or money's worth) the value of which is significantly less than the value of the consideration provided by the company.

five years ending with the commencement of the winding-up. On the other hand, a respondent suggested that no time limit should be set while a few others considered that the relevant time should be shorter, given the concern that a long look-back period would bring greater uncertainty to commercial arrangements by increasing the risk of invalidation by the courts.

11. We consider that a five-year look-back period is appropriate since it is consistent with the existing relevant provision for bankruptcy cases under the Bankruptcy Ordinance (Chapter 6) and the recommendation of the Law Reform Commission[7]. As regards the concern about the duration of the look-back period, we will emphasise that a transaction would only be caught by the provision under our current proposal if the court is satisfied that (a) at that time the company is unable to pay its debts or becomes unable to pay its debts as a result of the transaction; and (b) the value of the consideration received by the company is "significantly" less than the value of the consideration provided by the company. Besides, statutory safeguards would also be provided under our proposal such that the court would not make an order if it is satisfied that the company which entered into the transaction did so in good faith for the purpose of carrying on its business and there were reasonable grounds for believing that such transaction would benefit the company.

Proposal to enforce liabilities of liquidators notwithstanding their release by the court

12. To enhance the protection of creditors and strengthen the regulation of liquidators, we have proposed that a liquidator should not be absolved from liabilities under section 276 of C(WUMP)O[8] notwithstanding their release by the court *(Question 16)*.

13. The majority of respondents supported the proposal, although a few respondents objected to the proposal with the following reasons being cited –

(a) the risk of frivolous litigation against the liquidator is high given the nature of his work;

(b) as the liquidator's liability is personal, the proposal would result in uncertainty in relation to his subsequent liabilities and expose him to a very high level of personal risk; and

[7] Paragraphs 21.25-21.27 of the Law Reform Commission's Report on the Winding-up Provisions of the Companies Ordinance.

[8] Section 276 of C(WUMP)O provides that if it appears that any past or present liquidator of the company has become liable or accountable for any money or property of the company, or has been guilty of any misfeasance or breach of duty in relation to the company, the court may make orders to compel such person to repay or restore the money or property.

(c) the proposal would compel a liquidator to retain the books and records of a company indefinitely in order to be in a position to be able to defend himself against possible future claim.

14. Regarding (a), under our proposal, where the court has granted a release to a liquidator, an application under section 276 should only be made with the leave of the court to minimise the risk of frivolous litigation. In drafting the relevant provision, we intend to make reference to similar legislation in the United Kingdom ("UK"). There is already case law in the UK which could provide sufficient guidance for the court in exercising its discretion to grant leave and weed out frivolous litigations against the liquidator.

15. As regards (b), it should be noted that the proposal would bring the liability limitation period of liquidators in line with other professional sectors, where liability is subject to the limitation period set out in the Limitation Ordinance (Chapter 347)[9]. Liquidators should be able to manage the risk which they would be exposed, by taking out appropriate professional indemnity insurance.

16. In connection with (c), it should be noted that unless the court orders otherwise, a liquidator should not normally dispose of books and papers of a company immediately after his release. We consider that the situation of a liquidator is no different from that of another person working in a different professional capacity that should warrant more favourable treatment for liquidators.

Proposal to provide for civil liability of past directors and members in connection with a redemption or buy-back of shares out of capital

17. To safeguard against potential abuse and to ensure that a company's share capital is not returned to the members improperly prior to the insolvent winding-up of a company, we have proposed that where a company had redeemed or bought back its own shares by payment out of its capital and the company was wound up insolvent within one year of the redemption or buy-back, the recipient of the payment of the redeemed or bought-back shares and the directors who made the relevant solvency statement without having reasonable grounds for the opinion expressed in the statement should be jointly

[9] The limitation period would depend on the nature of the claim and is set out in the Limitation Ordinance (Chapter 347). For example, under section 31 of the ordinance, for an action for damages for negligence, the period is six years from the date on which the cause of action accrued, or three years from the date of knowledge (if that period expires later than six years from the date on which the cause of action accrued).

and severally liable to contribute to the assets of the company an amount not exceeding the payment in respect of the shares *(Question 31)*.

18. An overwhelming majority of respondents agreed with this proposal, although a few respondents expressed concern that in the case of listed companies, there might be practical difficulties in requiring the recipients of the payment of the redeemed or bought-back shares to make contributions (e.g. the difficulties in tracing such recipients), and that there might be unintended consequences for innocent parties. These few respondents suggested restricting the application of the proposal to connected persons or substantial shareholders for listed companies.

19. It should be noted that section 257 of the new CO provides that a listed company is prohibited from buying back its own shares by payment out of capital on an approved stock exchange. Therefore, a listed company may only buy back its shares by payment out of capital under a general offer or through a contract authorised in advance by special resolution. As the shareholders from whom the shares are bought back should be clearly identified in these situations, the question about practicability in tracing the members from whom the shares were brought back by listed companies should not arise.

20. As this proposal is intended to protect the interests of creditors by ensuring that the company's paid-up capital is preserved and not returned to its members immediately before the insolvent winding-up of the company, it is reasonable that it should apply uniformly to all companies being wound-up and all individuals who are recipients of the payment of the redeemed or bought-back shares. It would not be appropriate, as a matter of principle, to provide exemption for certain companies or certain categories of persons.

Proposals to improve efficiency and enhance the protection of creditors in a creditors' voluntary winding-up

21. We have proposed to –

(a) replace the existing requirement of holding the first creditors' meeting on the same or the next following day of the members' meeting for commencing a creditors' voluntary winding-up case with the requirement of holding the first creditors' meeting on a day not later than the fourteenth day after the day on which there is to be held the members' meeting *(Question 4)*;

(b) prescribe a minimum notice period of seven days for calling the aforesaid first creditors' meeting *(Question 5)*;

(c) limit the powers of the liquidator appointed by the members during the period before the holding of the first creditors' meeting *(Question 6)*; and

(d) provide that the powers of the directors would be restricted before the appointment of a liquidator *(Question 7)*.

22. The majority of respondents supported these proposals, which would ensure that reasonably sufficient notice is given to the creditors to prepare for the first creditors' meeting while reducing the time required for a company to commence a creditors' voluntary winding-up. On the other hand, a few respondents expressed concern that proposal (a) on its own would extend the potential time gap between the members' meeting and the first creditors' meeting to 14 days, which may provide a window for the directors and/or the liquidator appointed by the members to use the practice of "centrebinding"[10] to undermine the interests of creditors during the period.

23. It should be noted that if the existing requirement of holding the first creditors' meeting on the same or the next following day of the members' meeting is still in place (instead of adopting proposal (a)), the holding of the members' meeting for deciding whether to wind up a company voluntarily would need to be withheld in some cases in order to fulfil the proposed requirement for a seven-day notice period for calling the first creditors' meeting under our proposal (b). This is not satisfactory in case a company is in serious financial difficulty or insolvency, which calls for an early decision as to whether to commence the winding-up process.

24. In addition, proposals (c) and (d) would restrict the powers of both the directors and the liquidator appointed by the members during the 14-day period, thus effectively minimising the risk of "centrebinding" during the period. Besides, we have not received any similar feedback by creditors' groups expressing concerns that their interests might be undermined by the proposals. Indeed, proposals (a) to (d) are modelled on the relevant legislation in the UK, and no major concern has been expressed about its operation.

[10] "Centrebinding" refers to the practice whereby the company calls the members' meeting first to pass a winding-up resolution, deliberately puts off the holding of the first creditors' meeting and, with the aid of a liquidator appointed by the members at a members' meeting, does such things to the detriment of the creditors' interests, e.g. by selling the assets of the company at a knock-down price to a purchaser closely connected with the company or the directors. It derived its name from the case of *Re Centrebind Ltd* [1967] 1 W.L.R. 377, in which it was held by the UK court that prior to the holding of the first creditors' meeting, the members-appointed liquidator would have the powers to act as the liquidator of the company.

Priority of preferential payments in a winding-up

25. We received a few submissions on issues related to the winding-up regime which are of concern to the labour sector. A respondent suggested that employees should be accorded a higher priority than secured creditors and liquidators in terms of the distribution of assets in a winding-up. It should be noted that it is the basic principles of the corporate insolvency law of comparable common law jurisdictions (e.g. the UK, Australia and Singapore) that (a) the proprietary rights of a secured creditor over his security should generally not be interfered with by the liquidation process and that the security he has taken does not form part of the pool of assets for generating the fund for distribution amongst unsecured creditors; and (b) the liquidator's charges and liquidation expenses are generally payable out of the realised assets of the company in priority to other claims. In fact, under our existing legislation, employees are already accorded the highest priority amongst all unsecured creditors in relation to certain debts ahead of other preferential debts such as deposits in a bank winding-up and Government's statutory debts.

26. A respondent suggested that the current caps as set out in section 265 of C(WUMP)O for the payments that are to be preferentially paid to employees in priority to all other debts from the assets of the company in a winding-up[11] should be adjusted upwards to bring them to the levels of the relevant maximum amount of payment from the Protection of Wages on Insolvency Fund ("the PWIF")[12]. As the PWIF is entitled to a subrogated right in respect of the employees for such preferential payments, the respondent noted that adjusting the aforesaid caps upward would help replenish the PWIF.

27. It should be noted that any upward adjustment of the aforesaid caps in respect of employees' outstanding entitlements will affect the interests of other creditors by reducing the amount of realised assets available for distribution to them. A balanced view should be taken and it would not be appropriate to introduce any such change without considering the views of the other relevant stakeholders.

[11] Under section 265 of C(WUMP)O, the relevant caps for payments that are to be preferentially paid to employees in priority to all other debts from the assets of the company in a winding-up are $8,000 for outstanding wages and salary, $2,000 for wages in lieu of notice, and $8,000 for severance payment at present.

[12] The relevant caps of ex gratia payments from PWIF are $36,000 for arrears of wages; $22,500 for wages in lieu of notice; and $50,000 plus 50% of any excess entitlement for severance payment, etc.

The section 228A procedure[13]

28. An overwhelming majority of respondents supported maintaining the existing section 228A procedure for initiating a voluntary winding-up of a company, although a few proposed to repeal this procedure. The reason given by the latter was that if employees of a company which was wound up voluntarily under the section 228A procedure would like to apply for PWIF payments, they would first need to apply to the court for converting the case into a court winding-up, which is time-consuming and costly, given that the current ambit of PWIF only covers court winding-up cases.

29. It should be noted that the procedural considerations relating to winding-up cases initiated under section 228A are equally applicable to other creditors' voluntary winding-up cases. In this connection, we have consulted the public on a related issue in 2009/10, in the context of the consultation on the introduction of a statutory corporate rescue procedure, and the consultation conclusions at that time indicated that the risk of abuse and the rapid depletion of the PWIF[14] was the main concern in considering the question of whether the PWIF should be expanded to cover creditors' voluntary winding-up cases. Against this background, and noting that an overwhelming majority of respondents in the current consultation exercise supported retaining the section 228A procedure as a means to be used by the directors to wind up a company as a last resort, we have no plan to repeal the procedure.

WAY FORWARD

30. Backed by the overwhelming support for this legislative exercise, we will proceed to prepare the amendment bill with a view to introducing it into the LegCo in 2015. We will continue to engage relevant stakeholders as we prepare the amendment bill.

Financial Services and the Treasury Bureau
28 May 2014

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[13] Under section 228A of C(WUMP)O, if the directors have formed the opinion that the company cannot by reason of its liabilities continue its business, they may resolve at a meeting of the directors the matters and deliver to the Registrar of Companies a winding-up statement certifying the passage of this resolution. This procedure has the effect of allowing the directors of a company, in the absence of a resolution of the members of the company to do so, to commence a winding-up of the company voluntarily.

[14] Paragraph 61 in the Consultation Conclusions of Review of Corporate Rescue Legislative Proposals issued in July 2010. Please see http://www.fstb.gov.hk/fsb/ppr/consult/doc/review_crplp_conclusions_e.pdf.

Appendix I

List of Seminars and Meetings Attended

Date	Organising Party	Nature
17 April 2013	School of Law, City University Hong Kong	Lecture
3 May 2013	Legislative Council Panel on Financial Affairs	Meeting
9 May 2013	Hong Kong Institute of Certified Public Accountants and The Hong Kong Association of Banks	Seminar
15 May 2013	Asian Corporate Governance Association	Meeting
20 May 2013	The Chinese Manufacturers' Association of Hong Kong, The Chinese General Chamber of Commerce and Federation of Hong Kong Industries	Seminar
21 May 2013	The Law Society of Hong Kong	Seminar
22 May 2013	Financial Services and the Treasury Bureau and Official Receiver's Office	Forum
25 May 2013	Standing Committee on Company Law Reform	Meeting
19 June 2013	Hong Kong General Chamber of Commerce	Seminar
4 July 2013	The Hong Kong Federation of Trade Unions	Meeting
8 July 2013	The Hong Kong Institute of Directors	Seminar
18 July 2013	Business Facilitation Advisory Committee	Meeting

Appendix II

List of Respondents

1. Association of Chartered Certified Accountants
2. BDO Financial Services Limited
3. BRISCOE, Stephen
4. Chinese General Chamber of Commerce, The
5. Chinese Manufacturers' Association of Hong Kong, The
6. Consumer Council
7. CPA Australia
8. Federation of Hong Kong Industries
9. F T I Consulting
10. Hong Kong Association of Banks, The
11. Hong Kong Association of Restricted Licence Banks, The
12. Hong Kong Bar Association
13. Hong Kong Chinese Importers' & Exporters' Association, The
14. Hong Kong Exchanges and Clearing Limited
15. Hong Kong Federation of Insurers, The
16. Hong Kong Federation of Trade Unions, The
17. Hong Kong General Chamber of Commerce
18. Hong Kong Institute of Certified Public Accountants
19. Hong Kong Institute of Chartered Secretaries, The
20. Hong Kong Institute of Directors, The
21. Hong Kong Trustees' Association Limited
22. Hong Kong & Kowloon Trades Union Council
23. King & Wood Mallesons
24. Law Society of Hong Kong, The
25. Leader Corporate Services Limited
26. Linklaters
27. Office of the Privacy Commissioner for Personal Data, Hong Kong
28. New People's Party
29. PricewaterhouseCoopers
30. RSM Nelson Wheeler
31. ShineWing Specialist Advisory Services Limited
32. Society of Chinese Accountants & Auditors, The
33. YEUNG, Wai Sing, MH
34. 陳家和 (CHAN Ka-wo)
35. Zhonglei Specialist Advisory Services Limited
36. A respondent who has requested not to disclose his identity

Summary of Respondents' Views with Government's Responses

Item	Summary of Respondents' Views	Government's Responses
	Chapter 2 – Commencement of Winding-up	
A	***Providing for a prescribed form for a statutory demand by a creditor***	
	Question 1: Do you support the proposal to adopt a prescribed form of statutory demand, which would contain some key information as well as a statement of the consequences of ignoring the demand?	
	■ An overwhelming majority of respondents supported the proposal to adopt a prescribed form of statutory demand.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The specified amount of statutory demand should increase to $50,000 or even $100,000 to adjust for inflation over the years.	❖ The current amount was last increased in 2003 to $10,000 to bring it in line with the statutory demand for personal bankruptcy proceedings under the Bankruptcy Ordinance (Chapter 6) ("BO"). Besides, the corresponding figures in the UK and Australia are £750 and A$2,000 respectively, which are comparable to the amount in Hong Kong.
	❖ The statutory demand to be submitted by the petitioner should be accompanied with an affidavit (also in prescribed form) verifying that the debt is due and payable.	❖ Under the existing provisions in C(WUMP)O and Companies (Winding-Up) Rules (Chapter 32H) ("CWUR"), if a company fails to comply with the statutory demand within three weeks, the creditor may petition for the winding up of the company by the court and the petition is already required to be verified by an affidavit.
	❖ The prescribed forms of statutory demand as set out in the Bankruptcy (Forms) Rules (Chapter 6B) should be followed.	❖ Noted. We will take into account this suggestion when preparing the draft legislation.
	❖ The design of the prescribed form of the statutory demand should allow flexibility to facilitate settlement.	❖ Flexibility is already allowed by virtue of section 37 of the Interpretation and General Clauses Ordinance (Chapter 1) and rule 3 of CWUR.

Item	Summary of Respondents' Views	Government's Responses
	❖ From data protection point of view, it is prudent to confine the types of contact information to such personal data that is necessary for or directly related to the purpose of collection which is to enable contact to be established for the purpose of a statutory demand. Also, the personal data to be collected should be adequate but not excessive in relation to the purpose.	❖ As with the statutory demand for personal bankruptcy proceedings, the proposed prescribed form for court winding-up proceedings will only require the provision of personal data that is necessary for or directly related to the purpose of the statutory demand. Only the provision of correspondence address will be required in the prescribed form.
	■ A respondent suggested that the current non-prescribed form of statutory demand has worked well. A prescribed form may lead to disagreements with court clerks in their assessment of the certificate for compliance.	■ We do not agree that a prescribed form will give rise to such concerns. Indeed, for personal bankruptcy proceedings in Hong Kong, a prescribed form of statutory demand has already been adopted and has worked well in practice.
B	***Improving the section 228A procedure to reduce the risk of abuse***	
	Question 2: Do you think that the section 228A procedure, whereby the directors of a company may commence a voluntary winding-up of the company without first having the members of the company resolve to do so, should be maintained or repealed? *Question 3: If the section 228A procedure is to be maintained, do you agree to the proposed improvement measures as set out in the consultation document to reduce the risk of abuse of the procedure?*	
	■ An overwhelming majority of respondents were of the view that the section 228A procedure should be maintained. All respondents supported the proposed improvement measures for reducing the risk of abuse of the section 228A procedure as set out in paragraph 2.14 of the consultation document.	■ We are pleased to note the respondents' support for maintaining the section 228A procedure. We are pleased to note the respondents' support for the proposal to reduce the risk of abuse of the section 228A procedure and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ A mechanism should be made available to assist directors to preserve the assets of the company such as	❖ Winding-up under the section 228A procedure is in the form of a creditors' voluntary winding-up. Provisions applicable to a creditors'

Item	Summary of Respondents' Views	Government's Responses
	allowing a moratorium on claims against the company until such time as decisions about the winding-up and the appointment of the provisional liquidator or liquidator are taken subsequently by the members and creditors.	voluntary winding up will apply and a moratorium is currently not provided in such proceedings.
	❖ There is no need to specify in the winding-up statement that the directors have already called members' meeting since the new CO has already set out the duty of directors and the articles of association of each company have specified how meeting should be called and the length of notice. It is not practicable to ask the directors to state in the winding-up statement that they had already called the meeting of the company pursuant to section 228A as the company should be in financial dire strait and a lot of problematic issues would have to be considered and resolved.	❖ The proposal to require that the winding-up statement must state that the directors have already called the meeting of the company is intended to bring forward the requirement for calling the meeting of the company. As the company is already in financial dire strait, the members of the company should be informed of the financial condition of the company as soon as possible. Under our proposal, members of the company will be made aware of the directors' initiation of the section 228A procedure at the earliest possible instance.
	❖ The directors should inform members of the company of the winding-up and provide the reasons for the winding-up. This is to ensure that the members are duly informed and to reduce the risk of abuse.	❖ Our proposal is addressing this comment by ensuring that members are informed as soon as possible that directors have initiated the section 228A procedure.
	❖ Since some directors may simply state that "the company cannot by reason of its liabilities continue its business" is the only reason for winding up the company in the winding-up statement, requirements should be imposed to provide further details on the affairs of the company and explanation as to why any other modes of winding up is impracticable if not impossible to protect the interest of the creditors.	❖ Section 228A(2) already requires directors to specify in the winding-up statement the reasons to support their opinion that it is necessary to wind up the company and that the winding-up should be commenced under section 228A because it is not reasonably practicable for it to be commenced under another section of the ordinance. The specified form for the winding-up statement (Form NW2) also contains the same requirement.

Item	Summary of Respondents' Views	Government's Responses
	❖ There is a need to consider whether the winding-up statement should be subject to review and acceptance for filing by the Registrar of Companies ("R of C"). The winding-up of the company and appointment of provisional liquidator could, under such proposal, take effect only at the time of the acceptance of the winding-up statement by R of C rather than at the time of the delivery of the winding-up statement to the Companies Registry ("CR").	❖ Where a winding-up statement is delivered to R of C, the statement is considered as having been delivered at the time of acceptance even though the document is only placed on the register at a later time. However, according to section 35 of the new CO, if R of C refuses to register the statement, the statement is then retrospectively treated as not having been delivered and the winding-up is then treated as not having commenced.
	❖ Aggrieved creditors who are dissatisfied with the provisional liquidator's or liquidator's acts and dealings in the course of the winding-up under section 228A should be expressly given a right to apply to the court for an order to place the company into compulsory liquidation and appoint another liquidator.	❖ The right for creditors to petition for the winding-up of a company by the court when the company is in voluntary winding-up is already provided under section 257 of the C(WUMP)O.
	❖ Measures should be introduced to ensure that only duly qualified insolvency practitioners can be appointed as provisional liquidators under the section 228A procedure.	❖ Section 228A(8)(b) of the C(WUMP)O already provides that only a solicitor or a certified public accountant is qualified for taking up appointment as a provisional liquidator under the section 228A procedure.
	❖ A person should be allowed to accept the appointment of section 228A liquidator if he- • is the insolvency practitioners registered under the Panel A Scheme operated by the OR; or • has a recognised insolvency qualification from another jurisdiction; or • holds the specialist designation awarded by the Hong Kong Institute of Certified Public Accountants ("HKICPA"). There should also be an option for individuals to apply to and/or be approved to take up such appointments by either the OR, the R of C or the court.	❖ As the members of the company are not involved when the directors initiate the section 228A procedure, extra safeguards, e.g. in terms of the qualification of the provisional liquidator being appointed, should be provided in the law to prevent abuse of the procedure by directors. The Panel A Scheme is an administrative arrangement administered by the OR which applies only to court winding-up cases as the OR plays a specific role in court winding-up cases.

Item	Summary of Respondents' Views	Government's Responses
	❖ As an additional safeguard, directors should be required to make a statutory declaration of the matters stated in section 228A(1).	❖ There are already safeguards provided under section 349 of the C(WUMP)O and section 36 of the Crimes Ordinance (Chapter 200) which impose sanctions against a false statement made by directors.
	■ Two respondents proposed removing the section 228A procedure. One of them noted that the procedure is a form of voluntary winding-up and affected employees would first need to apply to the court for converting the case into a court winding-up in order to be qualified for ex gratia payment from the PWIF, which is time-consuming and costly.	■ We note that such concerns are actually not restricted to winding-up cases initiated under section 228A, but are equally applicable to other creditors' voluntary winding-up cases. In fact, during the consultation on the introduction of a statutory corporate rescue procedure in 2009/10, we have proposed expanding PWIF to cover creditors' voluntary winding-up cases. However, the Labour Advisory Board, the PWIF Board and some labour sector representatives had clearly voiced their strong objection to including creditors' voluntary winding up cases under the PWIF for fear of abuse and rapid depletion of the PWIF.
C	***Improving efficiency and enhancing the protection of creditors in a creditors' voluntary winding-up by improving the meeting arrangement of the members' meeting and the first creditors' meeting***	
	Question 4: Do you agree to replacing the existing requirement of holding the first creditors' meeting on the same or the next following day of the members' meeting with the requirement of holding the first creditors' meeting on a day not later than the fourteenth day after the day on which the members' meeting is held in a creditors' voluntary winding-up case? *Question 5: Do you support the proposal on prescribing a minimum notice period for calling the first creditors' meeting in a creditors' voluntary winding-up case? If so, do you consider a period of seven days appropriate?* *Question 6: Do you agree to the proposal on limiting the powers of the liquidator appointed by the company during the period before the holding of the first creditors' meeting in a creditors' voluntary winding-up case?* *Question 7: Do you agree to the proposed restrictions on the exercise of the directors' power before a liquidator is appointed in a creditors' voluntary winding-up case?*	
	■ A majority of respondents supported the proposal to provide that the company shall summon the first creditors'	■ We are pleased to note that the majority of respondents support the proposals. We will proceed with including the proposals in the draft

Item	Summary of Respondents' Views	Government's Responses
	meeting for a day not later than the fourteenth day after the day on which there is to be held the members' meeting in a creditors' voluntary winding-up. All respondents supported prescribing a minimum notice period for calling the first creditors' meeting. The majority also agreed that the minimum notice period should be seven days. The overwhelming majority of respondents supported the proposals as set out in paragraphs 2.23 and 2.24 of the consultation document to limit the powers of the liquidator appointed by the company before the holding of the first creditors' meeting and those of the directors before a liquidator is appointed.	legislation.
	■ Other comments raised by individual respondents include- ❖ Section 241(5) of the C(WUMP)O provides that if the meeting of the company at which the resolution for voluntary winding up is to be proposed is adjourned and the resolution is passed at an adjourned meeting, any resolution passed at the meeting of the creditors shall have effect as if it had been passed immediately after the passing of the resolution for winding up the company. If the proposals are adopted, consideration should be given whether section 241(5) should be amended accordingly. ❖ The minimum notice period for the creditors' meeting should be specified in business days rather than calendar days. ❖ The prescribed minimum notice period for the creditors'	❖ This will be a consequential amendment to our proposal. Section 241(5) will be amended to expressly provide that it will only apply in the case where the company's meeting is to be adjourned to a day later than the first creditors' meeting. ❖ Section 571 of the new CO provides that the requirement of giving notice for calling meetings is specified in calendar days. We suggest adopting a consistent approach. ❖ As the first creditors' meeting is to be held not later than 14 days after

Item	Summary of Respondents' Views	Government's Responses
	meeting should be set at more than 7 days (e.g. 10 or 14 days) or less than 7 days (e.g. 3 days).	the members' meeting under our proposal, prescribing a 7-day minimum notice period is appropriate. This is also consistent with the requirement for the summoning of a general creditors' meeting under CWUR and the relevant UK and Australian provisions.
	❖ The new legislation should require the company to give notice by instantaneous and publicly accessible means (e.g. email, facsimile and the company's website) to the extent it is practicable, in addition to "by post" as currently required by section 241(1) of C(WUMP)O.	❖ Part 18 of the new CO (Communications to and by Companies) is applicable to the sending of notice of creditors' meeting under section 241(1) of the C(WUMP)O. In addition to giving notice "by post" as required under section 241(1), the company may also give notice under 241(1) by email, facsimile or via the company's website, if agreed by the creditors.
	❖ For more effective oversight, only professionals e.g. practicing solicitors or accountants etc. should be qualified for appointment as liquidator in a creditors' voluntary winding-up. Nevertheless, it is suggested that SMEs should be exempted from this requirement so as to avoid the situation where SMEs cannot afford the fees of the relevant professionals due to insufficient assets.	❖ In general, C(WUMP)O does not impose any specific qualification requirement for appointment of liquidator, except for a winding up commenced under the section 228A procedure. At present, section and 255 of C(WUMP)O already contain provisions for oversight of a liquidator in a creditors' voluntary winding-up. In addition, section 276 of C(WUMP)O provides that if any liquidator has misapplied or retained any money or property of the company, he should be held liable and accountable for such money or property.
	❖ Powers of directors must cease once the company enters into liquidation. A provisional liquidator must be appointed if the shareholders wind up the company; and at the same time directors are allowed to continue making decisions for and managing the company.	❖ We agree that directors' powers should cease once the company enters into liquidation, except for disposal of perishable goods or preservation of the company's assets. Upon entering into liquidation, the existing directors should hand over the administration of the company's affairs to a duly appointed liquidator as soon as possible. Under our proposal, where the members have resolved to wind up the company voluntarily but no liquidator has been appointed by the company in a members' meeting, the powers of the directors shall not be exercised except with the sanction of the court or so far as may be necessary to secure compliance with the statutory requirements for the company to proceed with the creditors' voluntary winding-up.

Item	Summary of Respondents' Views	Government's Responses
	❖ If the powers of directors are restricted after commencement of liquidation but prior to appointment of a liquidator, it is questionable whether the director can charge for the work done.	❖ This is a matter that is subject to the agreement between the directors and the company, and is outside the scope of our proposals.
	■ Some respondents disagreed with the proposal that the company shall summon the first creditors' meeting for a day not later than the fourteenth day after the day on which the members' meeting is held. They submitted that the present requirement of holding the two meetings on the same or the next following day works well. They also expressed concern that this would extend the potential time difference between the two meetings, which could disadvantage the creditors and may open the situation to abuse, including increasing the chance of "centrebinding".	■ Our proposals are to ensure that reasonably sufficient notice is given to the creditors to prepare for the first creditors' meeting while not delaying the time for passing the resolution for winding up the company at the members' meeting. By allowing the company to summon the first creditors' meeting for a day not later than the fourteenth day after the day on which the members' meeting is held, the members' meeting can be summoned forthwith without being withheld until the first creditors' meeting is ready to be held. The risk of "centrebinding" can be minimised by introducing the safeguards as set out in paragraphs 2.23 and 2.24 of the consultation document by limiting the powers of the liquidators and directors in the interim period.
	<u>Chapter 3 – Appointment, Powers, Vacation of Office and Release of Provisional Liquidators and Liquidators</u>	
A	***Expanding the list of persons disqualified for appointment as liquidator or provisional liquidator***	
	Question 9(a): Do you agree to the expansion of the list of disqualified persons from being appointed as a provisional liquidator or a liquidator? If so, do you agree with disqualifying the types of persons as proposed in paragraphs 3.13, 3.15 and 3.16 of the consultation document?	
	■ An overwhelming majority of respondents supported the proposal to expand the list of persons disqualified for appointment as liquidator or provisional liquidator.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ When compared with the proposed definition of	❖ The provisions on disqualifications for appointment as provisional

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	"associate" for the provisions on voidable transactions, it can be construed that a spouse, cohabitant and relative should also be included in the list of disqualification of appointment.	liquidator or liquidator and those on voidable transactions serve different purposes. The policy intention of the disqualification proposal is to disqualify persons having a direct conflict of interest with the company from taking up the appointment of provisional liquidator or liquidator, and our present proposal strikes a reasonable balance between minimising conflict of interest situations and maintaining a sufficient pool of eligible persons for taking up such appointments.
	❖ In line with practices in Australia, a person should be forbidden from taking on an appointment as a liquidator if the prior relationship (a) is material to the insolvency; (b) has real potential for a litigation claim against the person by a stakeholder; or (c) is related to structuring of financial affairs of the entity in order to avoid the consequences of insolvency.	❖ Similar to the Australian practice, the HKICPA has set out similar guidelines in Hong Kong in its "Professional Ethics in Liquidation and Insolvency" under the "Code of Ethics for Professional Accountants". We consider it more appropriate to set out such general guiding principles and good practices in professional codes instead of codifying them in the draft legislation.
	❖ Some firms provide auditing, tax, company secretarial, corporate finance and other services to many listed companies, as well as insolvency practices. Creditors' choice of liquidators should not be unnecessarily restricted, or their costs unnecessarily increased, by new legislation under which leave of the court will be required in many cases for appointing insolvency practitioners from those firms.	❖ The categories of persons to be disqualified under our proposals are confined to those who, by virtue of their relationship with the company, are generally considered to be highly susceptible to being in a conflict of interest situation if acting as a company's provisional liquidator or liquidator. To cater for special circumstances and to avoid unnecessarily restricting the choice of provisional liquidator and liquidator, the proposal provides for such categories of persons to accept the appointment if leave is obtained from the court.
	❖ A person who has been an auditor of a company at any time up to six years (instead of two years as proposed) before the commencement of winding-up should be disqualified from acting as the liquidator of the company since six years is the general limitation period for civil proceedings.	❖ We consider that a two-year disqualification period for auditor is appropriate and represents a reasonable balance between minimising conflict of interest situations and maintaining a sufficient pool of eligible persons for taking up such appointments. We also note that the two-year disqualification period is in line with the existing Code of Ethics for Professional Accountants issued by HKICPA.

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	❖ As a receiver/receiver and manager is appointed by a financial creditor, it is understandable if financial creditors take the view that because a receivership is a private appointment, there is no compelling reason to disqualify a receiver/receiver and manager (without more) from being appointed as the provisional liquidator or liquidator.	❖ A receiver/receiver and manager appointed by a creditor pursuant to a security document acts for the primary interest and benefit of that creditor. A liquidator, on the other hand, acts for the interest of the general creditors as a whole. Due to the close connection between the appointing creditor and the receiver/receiver and manager, there is a perceived conflict of interest and lack of independence if such receiver is appointed as the liquidator. Therefore, under our proposal, a person who is currently a receiver/receiver and manager of a company should not be appointed as the liquidator of that company except with the leave of the court.
	❖ A court-appointed receiver, who needs to act impartially and under the direction of the court, should not be considered to have a conflict of interest and should not be disqualified from appointment as a provisional liquidator or liquidator in a court winding-up and a creditors' voluntary winding-up.	❖ While a court-appointed receiver would act under the directions of the court, the objective of his appointment by the court may be different or even in conflict with the interests that a liquidator is required to take care of. As such, it is more appropriate to leave it to the court to decide whether the receiver may be appointed as a liquidator.
	❖ Following section 500 of HKICPA's Code of Ethics for Professional Accountants, a respondent noted that it would not be appropriate to allow an auditor to accept an appointment as provisional liquidator or liquidator even with the leave of the court. Similarly, it would not be appropriate to allow a director of a company to be appointed as liquidator even with the leave of the court. On the other hand, another respondent suggested that persons subject to the proposed disqualified requirements due to conflict of interest might have intimate knowledge or information relating to the company, and therefore it would save substantial time and costs in the liquidation if they are appointed as liquidators.	❖ There may be some exceptional circumstances which justify a person falling within one of the categories of disqualified persons to take up an appointment as a provisional liquidator or a liquidator. To cater for such exceptional circumstances, we will provide in the draft legislation that these persons may accept such appointments with the leave of the court.

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	A respondent also made a general remark that the validity of the appointment of persons having potential conflict of interest should instead be dealt with on a case-by-case basis.	
	❖ Some respondents suggest that the new legislation should clearly specify the effect of a court finding or declaration that an appointment is void, as the office-holder might have done various kinds of practically irreversible things (e.g. dismissing employees) before his appointment is challenged. In particular, a respondent noted that if a liquidator is adjudicated bankrupt, or found mentally incapacitated, or subject to guardianship, section 278 of the C(WUMP)O should be made clear that he should be discharged automatically as a liquidator and his acts would be void.	❖ Noted. At present, rule 155 of the CWUR provides that if a bankruptcy order is made against the liquidator, he shall thereby vacate his office and shall be deemed to have been removed. Under our current proposal, we will update the said provision and extend it to cover mentally incapacitated persons, persons subject to guardianship and persons having conflict of interests. As to the validity of acts of a liquidator, there will be no change to the present position under section 196(5) of C(WUMP)O, namely the acts of a liquidator shall be valid notwithstanding any defects that may afterwards be discovered in his appointment or qualification. In order to protect the interest of a third party dealing with such a liquidator, there will also be provisions to the effect that the acts of such a liquidator would be considered valid despite the fact that it is afterwards discovered that he has vacated his offices.
	❖ The disqualification requirements should not be codified in the primary legislation. Instead, it should be set out in a subsidiary legislation to facilitate future modifications.	❖ At present the disqualification requirements of a liquidator are provided in section 278 of the C(WUMP)O. The respondent's suggestion would represent a fundamental change from the present framework, and we do not consider it appropriate to do so.
	❖ A licensing system for insolvency practitioners is strongly recommended to regulate the appointment of suitable persons as provisional liquidators or liquidators to enhance the regulatory functions and maintain a pool of sufficiently qualified and experienced insolvency practitioners to take up formal insolvency engagements.	❖ Given the relatively small market in Hong Kong and the limited number of practitioners involved, our view is that it may not be cost-effective to introduce a statutory licensing system to regulate the activities of practitioners.

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	❖ Creditors dissatisfied with incompetent and/or unprofessional insolvency practitioners should be able to voice their concern and bring about changes in their appointment economically and efficiently, with minimal need for court intervention given the costs of a formal application (for example under section 200(5) of the C(WUMP)O).	❖ To enhance the creditors' powers in the winding-up process, we have proposed, under Technical Proposal 6 in our consultation document, that a liquidator in a creditors' voluntary winding-up (except a liquidator appointed by the court or by direction of the court) may be removed by a creditors' meeting specially convened for the purpose. For liquidators appointed by the court or by direction of the court (in any type of winding-up), we consider it more appropriate to maintain the existing arrangement that the liquidator can only be removed by the court.
	❖ The disqualification proposal to expressly provide that a person subject to a disqualification order under Part IVA of C(WUMP)O would not be qualified to take up the appointment of provisional liquidator or liquidator should extend to disqualification orders made under all other Hong Kong ordinances.	❖ Section 168R of the C(WUMP)O already provides for the definition of "disqualification order" to cover the disqualification orders under Part IVA of C(WUMP)O and other Ordinances e.g. the Securities and Futures Ordinance (Chapter 571) ("SFO") and the repealed Securities (Insider Dealing Ordinance) (Chapter 395).
	Question 9(b): Do you agree to provide clearly that the appointment of a disqualified person as a provisional liquidator or liquidator shall be void and that he shall be liable to a fine if he acts as a provisional liquidator or liquidator?	
	■ An overwhelming majority of respondents supported the proposal to provide clearly that the appointment of a disqualified person as a provisional liquidator or liquidator shall be void and that he shall be liable to a fine.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ Where the appointment of the provisional liquidator or liquidator becomes void, the committee of inspection ("COI") or the creditors at general meeting shall within say 21 days appoint a replacement provisional liquidator or liquidator whose appointment shall take effect retrospectively from the date the appointment of the former provisional liquidator or liquidator becomes	❖ At present, whenever there is a vacancy in the office of provisional liquidator or liquidator (including a vacancy that arises because the appointment of a liquidator or provisional liquidator is void), the creditors or contributories (as the case may be) should promptly initiate the procedure to appoint another person to fill the vacancy as soon as possible to safeguard their interests. The existing law already provides that the OR shall by virtue of his office be the liquidator

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	void. Alternatively, there should be provision that the OR shall be the "default" provisional liquidator or liquidator during the period when there is no incumbent provisional liquidator or liquidator. ❖ The law should state clearly whether the disqualified provisional liquidator or liquidator will be indemnified by the estate of the company or he will be personally liable for his decisions made or contracts entered into on behalf of the company.	during any vacancy in a court winding-up. There is no intention to change the present legal position. ❖ As the provisional liquidator or the liquidator should continue to be held accountable for his actions notwithstanding that his appointment was or has become void, we consider it not appropriate to make specific provision in the C(WUMP)O to the effect that the liquidator will be indemnified for the decisions or contracts he made.
	■ Some respondents suggested that statutory defence should be provided for the offence in relation to the taking up of an appointment as provisional liquidator or liquidator by a disqualified person. In particular, they expressed that a fine should not be imposed on a disqualified person who acts as a provisional liquidator or liquidator if he is (i) not provided with full information or (ii) misrepresented by the management in assessing whether he is qualified to take up the appointment.	■ We consider it not appropriate to provide for a statutory defence for the said offence as a prospective provisional liquidator or liquidator should be in the best position to know his condition (e.g. being an undischarged bankrupt) and his relationship with the company (e.g. director, debtor or creditor) given that the proposed disqualification requirements are based on objective facts. As a matter of fact, non-compliance with the equivalent provision in Australia is a strict liability offence.
	Question 9(c): Do you agree that the disqualification proposals should also apply to the appointment of a receiver or a receiver and manager of the property of a company with suitable modifications?	
	■ Respondents' views are divided. Respondents who disagreed with the proposal cited the following reasons- ❖ Since a receiver or a receiver and manager is accountable to the party that appoints him, there is no need to extend, in the statute, the disqualifying proposals to the appointment of a receiver or a receiver and manager. ❖ It does not seem that it is fair or appropriate to	■ Noted. As a receiver/receiver and manager is generally appointed by the security holder and he should mainly be accountable to the party that appoints him, imposing the proposed disqualification requirements would restrict the appointment of a receiver by the creditor which in most cases is the security holder of the company. Therefore, having regard to the comments received, we will not propose any change to the existing position regarding the appointment of a receiver or a receiver and manager.

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	disqualify a creditor for appointment as receiver as it is the creditor who has the most substantial interest in the assets of the company.	
	■ A respondent suggested that the list of disqualified persons should also apply to the appointment of provisional supervisors.	■ The proposals to introduce a statutory corporate rescue procedure are being examined separately. This comment will be taken into account in that context.
B	***Disclosure of relevant relationships in relation to the appointment of provisional liquidators and liquidators***	
	Question 10(a): Do you agree that a new statutory disclosure system should be introduced for the appointment of provisional liquidators and liquidators?	
	Question 10(b): Do you agree with the details of information required to be disclosed as set out in paragraph 3.21 of the consultation document?	
	■ An overwhelming majority of respondents supported the proposal to introduce a new statutory disclosure system with criminal sanction.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ An extensive, but non-exhaustive, list of related parties and relationships should be provided in the law instead since any list of disclosable relationships may be treated as exhaustive while other potential conflict situations and relationships not on the list may be viewed as acceptable.	❖ Our proposal is a new requirement intended to improve the transparency of the appointment procedure of a provisional liquidator or liquidator. Since a failure to include a relevant relationship in the disclosure statement will constitute a criminal offence, it is necessary to set out the relationships that are required to be disclosed in a precise and readily ascertainable manner.
	❖ Some of the relationships included in the list of disclosable relationships are those that would result in disqualification and others are not. The disclosure proposal seems to suggest that persons disqualified from seeking appointment would, nevertheless, be able	❖ The scope of coverage under the disclosure requirements is wider than that under the disqualification requirements. For a person with a relationship that is listed in both the disqualification and disclosure requirements (e.g. a former auditor of the company before winding-up commences) who wishes to act as a liquidator of a company which is

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	to obtain approval for appointment from the creditors in a creditors' voluntary winding-up, whereas the disqualification proposal suggests that leave of the court would be necessary.	under a creditors' voluntary winding-up, he would be required to both (a) secure the court's sanction for acting as the liquidator of the company; and (b) disclose the said relationship in the statement of relevant relationships to be provided to the parties making the appointment.
	❖ In order to provide greater clarity and assist in compliance with the law, there should be a standard format for the proposed statement of relevant relationships.	❖ We intend to allow for flexibility by not providing a prescribed form of statement of relevant relationships. This would facilitate prospective liquidators to provide further details on the relevant relationships or any other submission in respect of his appointment to the appointing party for consideration.
	❖ The perceived conflict of interest should be considered with reference to Section 500 of the "Code of Ethics for Professional Accountants" issued by the HKICPA.	❖ In formulating the proposal on disclosure of relevant relationships, we have taken into account relevant requirements in other jurisdictions and other relevant references, including the HKICPA's Code of Ethics for Professional Accountants.
	❖ Due consideration must be given as to whether the justification for identifying the real or perceived conflict of interest or duty shall override the personal data privacy protection afforded to a prospective provisional liquidator or liquidator. When assessing the proper balance to be struck, the key point is whether the non-disclosure of such facts or relationships will likely prejudice the interests of creditors or others in the winding-up proceedings.	❖ The objective of the proposal is to ensure that the creditors will be able to make an informed decision on the appointment of a provisional liquidator or liquidator taking into account any potential conflict of interest associated with his relationship with the company. Under the current proposal, only necessary information is required to be disclosed to the data user (i.e. the appointing party) for the purpose of the appointment of the provisional liquidator or liquidator. The use of the personal data would be subject to the data protection principles set out in the Personal Data (Privacy) Ordinance (Chapter 486) ("PDPO").
	❖ The same disclosure requirements should be applied when a liquidator initially appointed under a members' voluntary winding-up is subsequently converted into a creditors' voluntary winding-up or a court winding-up because of insolvency. The appointment taker (originally under MVL) should be subject to the same	❖ Noted. We will provide in the draft legislation that when a members' voluntary winding-up is subsequently converted into a creditors' voluntary winding-up under section 237A of the C(WUMP)O, the current liquidator will be required to submit a statement of relevant relationships for tabling at a meeting summoned under section 237A for consideration of the appointment of the liquidator in the creditors'

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	disclosure requirements.	voluntary winding-up.
	❖ A respondent suggested that relevant relationships which have existed in the preceding six years prior to the appointment (instead of two years as proposed) should be covered as this is the general limitation period for civil proceedings. Another respondent suggested that the auditor of a company should disclose the relevant relationships for a longer period than two years preceding the commencement of the winding-up.	❖ The current proposal aims to facilitate the appointing party to make an informed decision on appointment of provisional liquidator or liquidator. Imposing a disclosure requirement on a prospective provisional liquidator and liquidator that covers certain relationships in the preceding two years is considered appropriate. The disclosure period of a prospective provisional liquidator or liquidator is not relevant to the general limitation period for civil proceedings.
	❖ With reference to the proposed definition of "associate" for voidable transactions, consideration should be given to extending the disclosure requirement to cover a cohabitant and a relative of the prospective liquidator.	❖ The current proposal on disclosure requirements covers an immediate family member (i.e. spouse, parent, child, sibling, grandparent or grandchild) of a director, secretary, auditor and liquidator, etc. For practicable reasons, the relationships that are required to be disclosed should be able to be verified by official records, "cohabitant" or "relative" are not included.
	❖ Some respondents made separate suggestions on further expanding the disclosure requirements to cover the following relationships- (a) a shadow director of the company or its holding company, subsidiary or fellow subsidiary; (b) any person whom a director can exert influence on; (c) a beneficial owner of the company or its holding company, subsidiary or fellow subsidiary; and (d) a nominee of the directors and/or shareholders in handling daily administration of the company or its holding company, subsidiary or fellow subsidiary.	❖ Our proposal would enhance the transparency of the appointment process for liquidators as compared with the existing regime, which does not impose a statutory requirement for prospective liquidators to disclosure relevant relationships. In drawing up the relationships which are required to be disclosed, we have made reference to the relevant Australian provisions. The respondents' suggestions would further expand the disclosure requirements in our proposals, and may increase the burden for the prospective provisional liquidator and liquidator to comply with such requirements.
	❖ The prospective provisional liquidator should be required to disclose if he is the immediate family	❖ Noted. As a receiver or receiver and manager of the company is familiar with the operation and the business of the company, we

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	member of a member, a creditor or a debtor, an employee, a receiver or a manager, a legal advisor of the company or the holding company or a subsidiary of the company.	consider it appropriate to extend the disclosure requirement to an immediate family member of a person who has, at any time within the immediately preceding two years, been a receiver or receiver and manager of the company's property. As noted above, further expanding the disclosure requirements may increase the burden for the prospective provisional liquidator and liquidator to comply with such requirements.
	❖ The new legislation should state with whom the disclosure statement has to be filed in addition to the creditors, such as the court, the OR and the R of C.	❖ Under our proposal, the statement of relevant relationships will be required to be delivered to the court (for a court winding-up) or tabled at the relevant meetings for the appointing party's consideration (for a creditors' voluntary winding-up) when appointing a provisional liquidator or liquidator. As the intention of the statement is to facilitate the appointing party to make an informed decision, we consider that it is unnecessary for the same to be filed with the OR or the R of C.
	❖ The definition for "financial advisor" and "legal advisor" should be made clear e.g. whether financial consultant, monitoring accountants, restructuring advisor/consultant should be regarded as "financial advisor".	❖ The terms "financial advisor" and "legal advisor" are widely used in daily language and have been adopted in some ordinances without assigning any specific meanings to them. The prospective liquidator or provisional liquidator should be in the best position to decide if he (e.g. being a financial consultant, monitoring accountants, restructuring advisor/consultant of a company) should be regarded as falling within any of the terms and make the relevant declaration.
	❖ Instead of primary legislation, the details of the disclosure should be set out in subsidiary legislation to facilitate future changes.	❖ The disclosure proposal is part and parcel of the package of proposals for improving the regime for the appointment of liquidators. As the current provisions on the disqualification of a liquidator are provided in section 278 of the C(WUMP)O, new disqualification and disclosure provisions should also be provided in the primary legislation.
	❖ A prospective provisional liquidator or liquidator should be required to attend the first creditors' meeting at which his appointment would be considered to answer	❖ If the first creditors' meeting agrees, a prospective provisional liquidator or liquidator may attend the meeting and answer any questions in respect of his relationships with the company. It is not

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	questions about any disclosable relationships. ❖ There may be practical difficulties in identifying all relevant relationships and obtaining the necessary information (e.g. in the liquidation of a large multi-national or overseas group of companies and where the company in liquidation has holding companies and subsidiaries).	appropriate to make it mandatory for him to attend a creditors' meeting. ❖ Our proposal already provides that it will be a defence for the prospective provisional liquidator or liquidator if he proves that he has made reasonable enquiries and, after making the enquiries, he has no reasonable grounds for believing that there existed such fact or relationship for disclosure in the statement of relevant relationships.
	Question 10(c): Do you agree that a statutory defence should be provided for a failure in disclosure?	
	■ All respondents supported introducing a statutory defence for a failure in disclosure.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ Defence should only be available where the prospective office-holder can prove he has made reasonable enquiries and, after making the enquiries, he is not aware of the relevant relationship concerned. If he is aware of it, he should disclose and explain why he considers there is no conflict. ❖ There is a need to clarify (a) whether or not the appointment of provisional liquidator or liquidator remains valid after deploying the defence; and (b) if so, what are the consequences to the liquidator for making inaccurate statement(s).	❖ The draft legislation will provide that the prospective provisional liquidator or liquidator must state the relevant relationships in the statement of relevant relationships and his reasons for believing that none of the relationships would result in a conflict of interest or duty. A defence would be available if he has made reasonable enquiries but was not aware of the existence of the relevant relationships. ❖ Under our proposal, once the provisional liquidator or liquidator becomes aware of an omission or error in the statement of relevant relationship, he is under a duty to make a replacement statement within a specified period to notify the relevant appointing party, and the appointing party may then accordingly decide whether or not to remove the provisional liquidator or liquidator. The appointment remains valid unless and until removal by the appointing party. Both the failure to include a relevant relationship and the failure to update a statement of relevant relationships are offences.

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	❖ There must be a mechanism in place for a liquidator acting in good faith to discharge his duties otherwise he may be sued by creditors (or other stakeholders) for damages.	❖ The proposal already provides that it will be a defence for the prospective provisional liquidator or liquidator if he proves that he has made reasonable enquiries and, after making the enquiries, he has no reasonable grounds for believing that there existed such fact or relationship for disclosure in the statement of relevant relationships.
C	***Expanding the existing prohibition on inducement affecting appointment as liquidator***	
	Question 11(a): Do you agree that the existing prohibition on inducement being offered to members or creditors in relation to the appointment of liquidators should be extended to cover inducement being offered to any person?	
	■ An overwhelming majority of respondents supported the proposal to extend the existing prohibition on inducement being offered to members or creditors to cover inducement being offered to any person.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The heading for the existing provision in the C(WUMP)O on the prohibition on inducement (section 278A of the C(WUMP)O) uses the term "corrupt inducement" but the section itself refers to "any valuable consideration".	❖ Noted. We will amend the heading of section 278A of the C(WUMP)O to more appropriately reflect the provisions under section 278A.
	❖ Under the HKICPA's Professional Ethics in Liquidation and Insolvency, there are two exceptions to the prohibition on offering or paying commissions (section 500.65), namely – (a) an arrangement between an insolvency practitioner and his practice's employee whereby the employee's remuneration is based in whole or in part on introductions obtained for the insolvency practitioner through the efforts of the employee; and	❖ Noted. We will provide for exceptions to the prohibition in the draft legislation in respect of the situations as set out in section 500.65 of the HKICPA's Professional Ethics in Liquidation and Insolvency.

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	(b) change of appointment resulting from transfer/sale of an existing practice due to e.g. the sale or merger of an insolvency practice or retirement of the outgoing insolvency practitioner (owner of the practice). The proposal should not cover these two types of situations.	
	❖ A few respondents were concerned that the extension of the coverage of the provision to "any person" may catch – (a) in-house cross-referrals between partners of the firm involving payment of referral fees should not be jeopardised; and (b) an insolvency practitioner offering lower charge-out rates to creditors even where this was done as part of a normal competition for business.	❖ Our proposal is consistent with the position in HKICPA's Professional Ethics in Liquidation and Insolvency, which regards that the payment or offer of any commission for, or the furnishing of any valuable consideration towards, the introduction of appointments as liquidators, provisional liquidators, special manager, receiver or manager, etc. as inappropriate. On the other hand, it is not the intention of our proposal to catch the offering of a lower charge in the normal course of business by an insolvency practitioner to secure an appointment, or the mere referral by one partner of a firm to another without any valuable consideration.
	❖ Consideration should be given to repeal section 278A in view of the paucity of case law.	❖ We consider it necessary to prohibit the inducement on appointment of liquidator and this section will therefore be retained. The proposal is modelled on the UK provisions.
	❖ Practical problems in implementation may arise e.g. there is currently no mechanism for filing and investigating such conduct.	❖ Under the existing mechanism, complaints in relation to non-compliance with section 278A may be filed to the Official Receiver's Office or the relevant authority for appropriate action.
	❖ Opportunity should be taken to amend section 278A so as to clarify what is and is not intended to be caught by the prohibition.	❖ Section 278A of the C(WUMP)O has existed for a number of years and the proposal is modelled on the relevant UK provisions. We have not proposed any change to the existing provision except for expanding the coverage from inducements being offered to

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		members/creditors to inducements being offered to any person.
	■ A respondent disagreed with the proposal and considers that as the members and the creditors are the only persons who can decide on the appointment of liquidator, it is not necessary to extend the existing prohibition to "any person".	■ Apart from the members or creditors of a company, other persons may influence the choice of liquidator e.g. members and creditors of the company may refer to or rely on any suggestion or recommendation made by the directors on the choice of liquidator. It is possible for directors who have received valuable consideration from a person to make suggestions or recommendations with a view to securing the corresponding person's appointment or nomination as the company's liquidator.
	Question 11(b): Do you agree that the prohibition should also be extended to inducement offered in relation to the appointment of provisional liquidators, receivers, and receivers and managers?	
	■ An overwhelming majority of respondents supported extending the existing prohibition on inducement in respect of the appointment of liquidators to the appointment of provisional liquidators, receivers, and receivers and managers.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ A respondent considered that prohibition should not be extended to (1) receivers and (2) receivers and managers as they are nominated and appointed by debenture holders.	■ A receiver is not just an agent of the debenture holders appointing him, but also has his equitable duties e.g. he owes a duty of care to the company in respect of the manner in which he decides to exercise a power of sale. Hence, the principle of prohibition of appointment by inducement is equally relevant to the appointment of receiver or receiver and manager of the property of a company. Similar prohibition is also found in the Australian provisions.
D	***Clarifying the nature of "provisional liquidators" in a court winding-up***	
	Question 12: Do you agree with the proposal to designate all provisional liquidators who take office upon and after the making of a	

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	winding-up order (i.e. section 194 PL) as "liquidators" such that they will be subject to the provisions in the C(WUMP)O which apply to liquidators?	
	■ A slight majority of respondents supported designating all provisional liquidators who take office upon and after the making of a winding-up order (i.e. section 194 PL) as "liquidators", but a number of respondents disagreed with the proposal due to the following reasons- ❖ The proposal will result in section 194 PL being given the full authority and powers of a liquidator upon and after the making of a winding-up order and he will be expected to take action accordingly. However, as he has not been confirmed by the creditors, and eventually may not be appointed, this would put the section 194 PL in office appointed immediately after the winding up order has been made at greater risk of being challenged by any successor liquidator who is appointed at a creditors' meeting. ❖ The section 194(1)(aa) provisional liquidators may not receive the approval of the creditors and contributories. If they are conferred with powers to carry out all the duties in the same way as liquidators, there is a risk that they would be able to carry on important matters (such as disposal of major assets) even before the creditors have considered and approved their appointment. ❖ The proposal could disincentivise the section 194 PL from calling an early creditors' meeting (given that the creditors may wish to appoint a different liquidator) and increase the risk of abuses, e.g., allowing assets to be sold off at less than market value to shareholders or	■ As acknowledged by a number of respondents, there is a need to provide more clarity in some of the existing provisions of the C(WUMP)O as to the extent to which they are applicable to section 194 PLs. Having regard to the concern of some respondents about our original approach for tackling the said issue (i.e. by designating all section 194 PLs as "liquidators"), we would adopt an alternative approach to clarify the application of the relevant provisions in C(WUMP)O to section 194 PLs so that the powers, duties and remuneration, etc. of such section 194 PLs would be more clearly spelt out in the legislation. Specific provisions include the following: - (a) <u>Where a person other than the OR who has been appointed under section 193 of C(WUMP)O as a provisional liquidator ("section 193 PL") acts as the provisional liquidator under section 194(1)(aa) ("section 194(1)(aa) PL"):</u> Having regard to the comments by some respondents that the powers of this type of section 194 PL should be restricted as the creditors have not yet given approval for his appointment and this person may not eventually become the "liquidator" of the company, we propose that a specific provision should be introduced to restrict the powers of this type of section 194 PL to those set out in section 199(4) to (6) of C(WUMP)O (i.e. same as in the case of (c) below); and (b) <u>Where the OR by virtue of her office becomes a provisional liquidator under section 194(1)(a) upon the making of the winding-up order:</u> The powers of the OR in her capacity as a section 194 PL in the present legislation would also be clarified to the effect that OR would have the powers of a liquidator as currently contained in section

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	directors. ❖ The proposal does not simply involve a change in terminology, but also a change in the powers of appointment takers. ❖ The status quo which is well understood and works effectively should be retained. However, most of the respondents who disagreed with the proposal acknowledged the existence of uncertainties over the application of certain provisions in the C(WUMP)O to different types of section 194 PLs , and suggested that greater clarity should be provided in the law.	199(1) and (2) of C(WUMP)O. (c) <u>Where one or more persons is/are appointed by the OR as provisional liquidator under section 194(1A) of the C(WUMP)O in place of himself under the existing "Panel T" scheme:</u> The powers of this type of section 194 PL are already set out in the existing section 199(4) to (6) of the C(WUMP)O and we do not propose any change in this regard.
	■ Other comments raised by individual respondents include- ❖ If the Government is standardising the title of the officer to "liquidators", it might be necessary to amend the titles of "provisional trustees" and "trustees" under the BO as well. ❖ The name of section 193 PL can be changed to e.g. "interim liquidator" or "provisional liquidator before winding up order" so that they can be differentiated from section 194 PL and the eventual "liquidator". ❖ The new legislation should avoid the word "continues" now found in section 194(1)(aa) of the C(WUMP)O. ❖ A mechanism should be implemented to allow for the petitioning creditor to nominate a liquidator in the petition document for winding-up or, alternatively, other	❖ The focus of the current legislative exercise is on improving the company winding-up provisions in the C(WUMP)O. The relevant provisions in the BO should be reviewed separately. ❖ Our revised proposal would address the issue of the application of the provisions in the C(WUMP)O to the different provisional liquidators and liquidators without designating section 194 PLs as "liquidators". ❖ Noted. We will amend section 194(1)(aa) of the C(WUMP)O accordingly. ❖ The benefit of the respondent's proposal is not clear. There are also practical difficulties in allowing the nomination of a liquidator before the court orders the winding-up of the company (e.g. the difficulties in

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	creditors can nominate a liquidator prior to the winding-up hearing.	ascertaining the identity and wishes of creditors and contributories).
	Question 13: Do you agree with the proposal to clearly stipulate that it is up to the court to determine the powers, duties, remuneration and termination of appointment of provisional liquidators who were appointed by the court before the making of a winding-up order (i.e. section 193 PL)?	
	■ A majority of respondents supported providing more clearly that it is up to the court to determine the powers, duties, remuneration and termination of appointment of a section 193 PL.	■ We are pleased to note the support for the proposal and will include it in the draft legislation accordingly.
	■ Other comments raised by individual respondents include- ❖ As the objective of the legislative exercise is to facilitate more efficient administration of the winding-up process, it would be more practicable to continue following the existing practices that have been effective so far. Section 193(3) of the C(WUMP)O has clearly stipulated that the court may limit and restrict the liquidators' powers by the order appointing him. In practice, the appointment order of provisional liquidators should have specified their powers. The requirement for taxation of agent's bill(s) in a section 193 PL should be covered in the statute.	❖ The existing legal position is that the powers, duties and remuneration (including expenses e.g. agents' bills) of a section 193 PL are determined by the court. It is intended that appropriate revisions would be made to the provisions in C(WUMP)O to make the position clearer. It will not change the legal position as set out in section 193(3) of the C(WUMP)O that the court may limit and restrict the liquidators' powers by the order appointing them. The proposal would also provide that it is up to the court to consider any application for termination of the appointment of such a section 193 PL.
E	***Modernising the provisions on the powers of liquidators***	
	Question 14: Do you agree with the proposal of setting out the powers of liquidators now found in section 199(1) and (2) of the C(WUMP)O in a Schedule to improve the clarity of the provisions?	

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	■ An overwhelming majority of respondents supported setting out the powers of liquidators in a Schedule to improve the clarity of the provisions.	■ We are pleased to note the support for the proposal and would include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The schedule should not be regarded as an exhaustive list and the liquidators should be able to apply to the court for additional powers for flexibility.	❖ Noted. Our proposal will not change the present scope of powers of a liquidator and the position that a liquidator may apply to the court for the exercise of the powers currently contained in section 199 of the C(WUMP)O.
	Question 15: Do you agree that the requirement for the liquidator to apply to the court or the COI for exercising the power to appoint a solicitor in a court winding-up should be removed, provided that prior notification is given to the COI or, where there is no COI, the creditors when the liquidator exercises such power?	
	■ An overwhelming majority of respondents supported removing the requirement for the liquidator to apply to the court or the COI for exercising the power to appoint a solicitor in a court winding-up.	■ We are pleased to note the support for the proposal and would include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The opportunity should be taken to harmonise the position with regard to the commencement of legal proceedings between court winding-ups and voluntary winding-ups such that a liquidator in a court winding-up will be allowed to commence legal proceedings without seeking court sanction.	❖ A court winding-up is generally under the supervision of the court. There is good reason for requiring prior court sanction (or sanction of the COI alternatively) for commencing legal proceedings. Since the commencement or continuation of legal proceedings is an important decision which is likely to have consequence on the estate as a whole (such as costs implication), requiring prior sanction for such a decision would ensure that the interests of the creditors are properly protected.
	❖ The COI/creditors should be allowed to give retrospective sanction to a liquidator for exercising powers under sections 199(1) and 199(2) of the C(WUMP)O. Under the current position, the liquidator can seek retrospective sanction from the	❖ We consider that it is more appropriate to require retrospective sanction to be given by the court instead of by the COI/creditors ,as the court is a just and independent third party which may decide whether ratification of the liquidator's conduct should be given after considering the circumstances of the case as a whole (including the

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	court, but this adds to the costs of the liquidation and does not benefit the creditors.	reasons behind the liquidator's failure to obtain prior sanction and the possible consequences of a decision, or a refusal, to grant a retrospective sanction on the parties affected – which are likely to include both the liquidator and the creditors) and make necessary orders in relation to the application as the court sees fit and appropriate. The requirement for retrospective consent to be given by the court instead of by the creditors or COI is consistent with case law.
	❖ The legislation should set out what a COI can do in case it has a different opinion from the liquidator regarding the proposed appointment of solicitors, such as whether it can apply to court, etc.	❖ Currently, section 199(3) of the C(WUMP)O expressly provides that any creditor or contributory may apply to the court with respect to the exercising or the proposed exercising of any of the powers conferred on the liquidator by section 199. Further, section 200(5) of the C(WUMP)O provides that any person who is aggrieved by any act or decision of the liquidator may apply to the court under that provision, and the court may confirm, reverse, or modify the act or decision complained of, and make such order as it thinks just.
	❖ The proposed legislation should stipulate the number of days that the liquidators have to wait to see whether there is objection from any COI members/creditors before appointing a solicitor.	❖ Noted. We will include an express provision in the draft legislation to the effect that liquidators are required to give notice to the COI members/creditors not less than 7 days before the exercise of the power to appoint a solicitor. In case the COI members/creditors consider necessary, they may challenge the liquidator's decision under section 199(3) or other provisions of the C(WUMP)O.
	■ A respondent disagreed with this proposal and pointed out that in a court winding-up, it is particularly important that the liquidator should be required to apply to the court or the COI for the exercise of the power to appoint a solicitor. To protect the interests of relevant company and creditors, the respondent suggested that section 199(1)(c) of C(WUMP)O should be retained.	■ As it is very common for a liquidator to engage a solicitor to assist him in the performance of his duties, and sanction is usually given for the liquidator to exercise the power to appoint one in a normal court winding-up case, there is room for streamlining the process. To strike a balance between the interests of different parties, the liquidator would be required to give notice to the COI or, where there is no COI, to the creditors 7 days in advance of his exercise of this power.

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		Under the C(WUMP)O, any creditor or contributory may apply to the court with respect to any exercise or proposed exercise of any of the powers under section 199. The law also provides that if any person is aggrieved by any act or decision of the liquidator, that person may apply to the court, and the court may confirm, reverse, or modify the act or decision complained of, and make such order in the premises as the court thinks just.
F	***Enhancing the regulation of liquidators by enforcing liabilities of liquidators notwithstanding their release by the court***	
	Question 16(a): Do you agree that, notwithstanding the release of a liquidator by the court, the liquidator should not be absolved from the provisions of section 276[1] of C(WUMP)O? *Question 16(b): Do you agree that, where the court has granted a release to a liquidator, the power to make an application under section 276 should only be exercisable with the leave of the court?*	
	■ A majority of respondents supported that the liquidator should not be absolved from the provisions of section 276 of C(WUMP)O notwithstanding the release of a liquidator by the court.	■ We are pleased to note the support for the proposal and would include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ Pursuant to section 290 of the C(WUMP)O, for a company which has been dissolved, the court has the power to declare the dissolution void within two years of the date of dissolution. A respondent suggested that since dissolution of a company and the release of liquidators are in many occasions interrelated, a similar	❖ Section 276 of the C(WUMP)O provides a summary procedure for enforcing a claim against wrongdoers which may be invoked where the company is in the course of winding-up. Where the company has been dissolved, section 276 proceedings can still be taken by restoring the dissolved company under section 290 of

[1] Section 276 of the C(WUMP)O provides that if, in the course of winding up a company, it appears that any past or present liquidator of the company has misapplied or retained or become liable or accountable for any money or property of the company, or has been guilty of any misfeasance or breach of duty or breach of trust in relation to the company, the court may examine into the conduct of such person and make orders against him to repay or restore the money or property or any part thereof, or to contribute such sum to the assets of the company by way of compensation in respect of the above delinquent acts.

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	time clause of two year should be incorporated into the proposed legislation when enforcing liabilities of liquidators. A few respondents also suggested that there should be consequential amendments to section 276 of the C(WUMP)O to ensure that it could be invoked even after the company has been dissolved.	the C(WUMP)O. While section 290 stipulates that the court has the power to declare a dissolution void within two years of the date of dissolution, the two-year time limit may be extended by the court if the court is satisfied that there are exceptional circumstances justifying the extension. The two-year time limit for restoration of a company under section 290 of the C(WUMP)O is not relevant to the time limit for an application under section 276.
	❖ A time limit should be imposed within which the liquidator would remain liable or accountable for any money or property of the company after the order releasing the liquidator is made.	❖ The time limit of the current proposal is subject to the law on limitation periods for commencing legal proceedings. The Limitation Ordinance (Chapter 347) already imposes different limitation periods for commencing different types of legal proceedings. It would not be necessary or appropriate to have a separate or concurrent legal provision on limitation periods for this proposal.
	❖ In cases where there is a change of liquidators or the resignation of a liquidator is followed by a replacement by another, it is in doubt whether all liquidators or only the last liquidator would be held responsible for all the decisions made during liquidation.	❖ Section 276 of the C(WUMP)O provides a procedure for enforcing existing liability against any past or present liquidator. A liquidator will be liable for his own conduct, and any change or resignation of the liquidator will not shift or discharge his liability.
	❖ Consideration should also be given to whether the proposal should extend to provisional liquidator as well.	❖ Noted. We will make appropriate amendments so that the proposal would also apply to provisional liquidator appointed under section 194(1A) or holding office by virtue of section 194(1)(aa) of the C(WUMP)O.
	■ Some respondents did not agree with the proposal as follows-	
	❖ Given the nature of a liquidator's work, it is likely that not all stakeholders will be happy with the situation and therefore the risk of frivolous litigation against the liquidator is high.	❖ Our proposal already provides safeguards. In order to strike a balance between minimising the risk of frivolous litigation and the need to protect the rights of creditors, contributories or other interested parties, it is proposed that any application under section 276 of the C(WUMP)O against a liquidator who has obtained his release from the

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		court should only be made with the leave of the court.
	❖ The liquidator's liability is personal. He cannot set up a limited liability vehicle through which he offers his services, as most other professionals can. This uncertainty in relation to subsequent liabilities and the lack of protection of the professional indemnity insurance ("PII") would expose liquidators to a very high level of personal risk.	❖ Liquidators may purchase PII to protect themselves against legal liability arising from professional negligence, errors or omissions. The situation of a liquidator is not different from that of another person working in a different professional capacity, whereas PII products are available for those professionals e.g. legal professionals.
	❖ A liquidator would not be able to dispose of the books and records of a company after release, but instead may feel compelled to retain indefinitely and store the records in order to be in a position to be able to defend himself against possible future claims.	❖ Like other professionals, a liquidator should not dispose of books and papers of a company or of a case right away after his release under normal circumstances.
	❖ The proposal to require that invoking section 276 proceedings against the liquidator exercisable only with leave of the court is no real safeguard. If there is any possibility of sustaining a case against a liquidator, a court would not have grounds to deny an application and the court would not be in a position to investigate the validity of details of the claim.	❖ In considering whether to grant leave, the court will carefully exercise its discretion and will take into account the facts and circumstances of the case. The proposal to require a court leave as safeguard is modelled on the relevant UK provisions and there is case law for reference.
	<u>Chapter 4 – Conduct of Winding-up</u>	
A	***Stipulating the maximum and a minimum number of members of the committee of inspection ("COI")***	
	Question 18: Do you agree that a maximum and a minimum number of members should be set for the COI appointed in both a court winding-up and a creditors' voluntary winding-up? If so, are the proposed maximum number (seven) and minimum numbers (three) appropriate? Do you agree that the court should have the discretion to vary the maximum and minimum numbers on application by the liquidator?	

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	Question 19: Do you agree to allow the COI not to fill a vacancy if the liquidator and a majority of the remaining members of the COI so agree, provided that the total number of members does not fall below the proposed minimum number?	
	■ The vast majority of respondents agreed that the maximum and minimum number of members of the COI should be set as seven and three respectively. They also agreed that the court should have the discretion to vary the maximum and minimum numbers. The vast majority of respondents supported the proposal on the filling of vacancy in a COI as stated in paragraph 4.10 in the consultation document.	■ In the light of overwhelming support for these proposals, we would proceed to include them in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ Age limit should be imposed for COI members.	❖ At present, the C(WUMP)O does not contain any restriction in respect of the age of COI members. The suggestion for imposing a limit on age is not sufficiently justified.
	❖ The present regime should be maintained which has the benefit of leaving the decision as to whether to appoint a COI and the number of its members to the creditors who are in the best position to decide this question.	❖ Our proposals suggest no change to the existing mechanism under which (a) the creditors and contributories may decide whether or not to apply to the court for an order appointing a COI in a court winding-up, and (b) the creditors may decide whether or not to appoint a COI in a creditors' voluntary winding-up. Setting the minimum number of COI members as three will minimise the chance of a deadlock of the COI. On the other hand, a large number of COI members may stifle the decision making process and therefore a maximum number of seven is proposed. To allow flexibility, the maximum and minimum number may be varied by the court.
	❖ Allowing the company to apply to the court to vary the maximum and minimum numbers of COI is impractical,	❖ Compared with the existing arrangements, the chance that the proposals would result in additional costly paper applications is not

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	as it would create further "paper" applications made to the court and would also impose an unnecessary burden on the company to incur costs in making such application.	high. Currently, in a court winding-up, an application to the court is already required for the appointment of a COI and the variation of the maximum and minimum numbers of COI could be dealt with in the same application. For a creditors' voluntary winding-up, the present law already effectively provides for a maximum and a minimum number of members. The present proposal would only amend these numbers in question.
	❖ There might be difficulty in seeking three COI members to meet the proposed minimum number. It would be more efficient to set the minimum number and maximum number of COI members at two and seven. It would be more flexible to leave the minimum number of COI members to the discretion of the stakeholders.	❖ To allow flexibility, the minimum number may be varied by the court upon application.
	❖ It was not clear why it is thought that seven members will facilitate the operation of the COI while the UK and the Australian legislation prescribe the maximum number of members of COI for not more than five. The maximum number of COI members should be set at five instead of seven as more time and costs will be incurred for a greater number of the COI members. In court winding-up cases, the court almost always appoints five or less COI members.	❖ While a COI consisting of five members may be suitable for some cases, it may be necessary in other cases (e.g. in large winding-up cases, especially those involving companies with international operations) to appoint more members to ensure that the COI is sufficiently representative of the general body of creditors. In any case, an application can be made to the court to vary the maximum for such cases.
	❖ If the COI member is absent from three consecutive COI meetings without the consent of other COI members (instead of five consecutive meetings under the C(WUMP)O), his office should be vacated.	❖ It is noted that the Australian provision requires a member of the COI to be absent from five consecutive meetings of the COI before his office becomes vacant. The current requirement is not considered to be unreasonable.
	❖ Instead of the proposed arrangement of not requiring the COI to fill a vacancy subject to the agreement of the	❖ A creditor or contributory who is interested in joining the COI may express interest to the liquidator at any time during a winding-up for

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	liquidator and a majority of the remaining COI members, the liquidator should notify the creditors and contributories of any proposal of not filling a vacancy of the COI with sufficient notice period. This would allow other creditors and contributories who did not join the COI previously to have a chance to participate.	the liquidator to make an appropriate decision taking into account circumstances of the case. In the case where a vacancy arises in the COI, under both the existing and the proposed provision, the liquidator is only exempted from the requirement to summon meetings of creditors and contributories if the liquidator (and the COI, if applicable), having regard to the position in the winding-up, is of the opinion that it is unnecessary for the vacancy to be filled. In any other cases, the liquidator must notify the creditors and contributories by calling the meetings to fill the vacancy.
B	***Streamlining and rationalising the proceedings of the COI***	
	Question 20: Do you agree to the proposals as set out in paragraphs 4.12 and 4.13 in the consultation document for streamlining and rationalising the proceedings of the COI? *Question 21: Do you support the proposal to enable the COI to function through written resolutions sent by post or using other electronic means (such as using emails or through websites)?*	
	■ All respondents agreed to the proposals as described in paragraphs 4.12 to 4.14 of the consultation document regarding the proceedings of the COI.	■ We are pleased to note the support for the proposals and would include them in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The current proposal should also include a provision stating that a meeting summoned according to the rules shall be presumed to have been duly summoned and held, notwithstanding that not all those to whom the notice is required to be given have received it.	❖ Rule 121 of CWUR is relevant to the meetings of creditors or contributories and is concerned with a meeting with potentially a large number of persons which does not apply in the context of COI. Having regard to the relatively small size of a COI, a provision stating that a meeting summoned according to the rules would be presumed to have been duly summoned and held is not considered appropriate.
	❖ It was suggested that a COI meeting might take place by remote attendance, in the form of video conference or other comparable means.	❖ Noted. The draft legislation will allow meetings of COI to be held in two or more places by the use of technology.

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	❖ It should be made clear in the law that a written notice by the liquidator to members of the COI can be given by electronic means.	❖ The draft legislation will provide that a written notice can be given by the liquidator to members of the COI by electronic means.
	❖ A mechanism allowing a COI to dispense with the audit requirement for liquidator's accounts should be introduced.	❖ In a court winding-up, the OR is empowered by section 203(3A) of C(WUMP)O to cause the liquidator's account to be audited at any time. Under section 203(5), the OR may decide that the account need not be audited. The power to cause the liquidators' accounts to be audited is essential for the regulatory role of the OR. The decision of whether audit is required should therefore fall on the OR instead of the COI in a court winding-up. In a voluntary winding-up, a COI is already empowered to dispense with the requirement for audit of the liquidator's accounts by virtue of section 255A of the C(WUMP)O.
	❖ The current requirement for the COI to certify that the liquidator's accounts are full, true and complete, may deter some COI members from signing off on the certificate. Rather than a certification by the COI, as in the current Forms 86 and 88 of the CWUR, it is suggested that COI be required to review the accounts and that the accounts can be taken as accepted if no committee member has any objection.	❖ We are not aware of any particular problem in complying with the existing requirement of certification of accounts. The certification requirement would help ensure the active involvement of COI in the administration of the winding-up and maintenance of close supervision of the liquidator's conduct, which in turn would enhance protection of the interests of the general body of creditors.
	❖ The waiver of the notice requirement for calling a COI meeting should be subject to approval of all members for the meeting.	❖ Under our proposal, in the event that the liquidator has failed to give proper notice to all COI members, waivers from all members are required. However, if the liquidator has only failed to give sufficient notice to a particular member, only the waiver by that member is required.
	❖ After the first COI meeting, a COI meeting should be called on request by at least two COI members.	❖ We do not consider it appropriate to restrict the existing right of a COI member or his representative to call a meeting.
	❖ The liquidator should discuss and agree with the	❖ Our proposal does not prohibit such an arrangement between the

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	members of COI on the preferred choice of communication methods at the first meeting of COI.	liquidator and the COI member. However, there is no intention to make this a mandatory requirement. It is not appropriate to restrict the making of any decision on the communication method.
	❖ A written resolution passed by a majority of the COI should be sufficient to carry a motion.	❖ Under the present proposal, a written resolution may be passed by a majority of the COI.
	❖ The current proposal does not introduce detailed rules determining how and when service of written resolution by post is considered to be effective and should be amended by including express provision that shall apply in relation to the service of written resolution by post.	❖ Noted. We will make reference to the relevant provisions of the new CO in setting out the details in the draft legislation.
	❖ It is not clear from the proposal whether the definition of "other electronic means" will include or exclude the use of facsimiles in addition to emails and websites. It is appropriate to specify an approved list of acceptable forms of electronic communication.	❖ It is the intention to allow communication by the liquidator by the use of facsimiles as well. However, given the rapid development of technology, we have reservation about specifying an approved list of acceptable forms of electronic communications and a more flexible approach will be adopted in drafting the provisions to enable the use of different forms of electronic communications.
C	***Simplifying the process for the determination of costs or charges of liquidators' agents in a court winding-up***	
	Question 22(a): Do you agree with allowing the costs and charges of the agents employed by the liquidators to be determined by agreement between the liquidator and the COI? *Question 22(b): Do you agree that if such agreement cannot be reached, the costs and charges of the agents shall be delivered up for taxation by the court?*	
	■ An overwhelming majority of respondents agreed to the proposal to allow the bills of costs or charges of the agents employed by the liquidator be determined by agreement with the COI. The respondents also agreed that if such agreement cannot be reached, the costs and charges shall	■ In view of the vast majority support for the proposal, we plan to proceed with including it in the draft legislation.

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	be delivered up for taxation by the court.	
	■ Other comments raised by individual respondents include- ❖ While the proposal would certainly save time and effort, SME creditors may not have sufficient knowledge to determine the reasonable costs and charges to reach the agreement with liquidators.	❖ The proposal aims to provide an alternative approach to agree on the costs or charges of liquidators' agents with a view to saving time and costs required for the taxation process. If the COI members are unable to reach an agreement with the liquidators, the liquidators are still required to use the existing mechanism in determining the costs or charges of the liquidators' agents.
	❖ A de minimis threshold should be set for allowing the costs and charges of the agents employed by the liquidator to be determined by agreement between the liquidator and the COI as in the taxation process.	❖ Introducing a de minimis threshold would complicate our proposal and may give rise to possible abuses (e.g. splitting of a bill into a number of bills falling below the threshold).
	❖ Consideration may be given to extending the powers of the COI to cover the remuneration of the provisional liquidators in a court winding-up and their agents costs and expenses incurred during the provisional liquidation if the company is subsequently wound up and a COI is appointed, and the provisional liquidators fees/agents costs have not been taxed by the court during the provisional liquidation period.	❖ A section 193 PL acts pursuant to the court order appointing him, and his remuneration is determined by the court. This section 193 PL does not really conduct the winding-up of the company as it is not yet clear whether an order for the winding-up of the company will ultimately be made. It is not appropriate to extend the powers of COI, which is appointed only when the company is being wound up, to determine the remuneration of this type of provisional liquidator during the provisional liquidation period prior to the making of the winding up order.
	❖ The liquidators should be required to provide similar level of information presently required of them to justify the costs and charges in a taxation save for the preparation of detailed bills of costs the preparation of which are time consuming and costly.	❖ Our proposal is to align the procedure for determining the costs or charges of the liquidators' agents with the existing procedure in relation to the determination of the liquidator's remuneration by agreement with the COI.

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	❖ Consideration should be given to extend the power of the OR to apply for review of the agreement reached between the liquidator and the COI on the agents' costs or charges.	❖ The spirit of the proposal is to provide an alternative by allowing the liquidator to agree with the COI on agents' costs. In case of any dispute, it could be resolved by the taxation procedure under the existing provisions in C(WUMP)O and CWUR. To provide further checks-and-balances, we will consider if it is necessary to extend such right to the OR.
	❖ The court should be given the power that in its discretion the costs or charges of agents or the remuneration of the liquidator can be assessed by the court "on papers" summarily.	❖ Our proposal provides an alternative to streamline the present procedure. The matter will continue to be determined by the court under the existing mechanism and following existing procedure in the absence of a COI or if the liquidator fails to agree with the COI on the bills of agents.
	❖ Only for costs and charges of agents charged at a fixed costs or a percentage or on a success fees basis should be determined by agreement between the liquidator and the COI. For all other agents who charged on hourly basis should go through the normal taxation process.	❖ The objective of the proposal is to streamline the present procedure by providing an alternative court-free approach to determine the costs and charges with a view to saving time and costs. If the COI members do not prefer to use this alternative approach, they can refuse to agree with the liquidator in which case the liquidator is still required to use the existing mechanism in determining the costs or charges of the liquidators' agents.
D	***Allowing communication by liquidators with creditors, contributories, members of COI and other interested parties by electronic means***	
	Question 23: Do you support the proposal to allow liquidators and provisional liquidators to communicate with creditors, contributories or other parties by electronic means, subject to the conditions as set out in paragraph 4.21 of the consultation document?	
	■ An overwhelming majority of respondents supported the proposal to allow electronic communication by liquidators to the relevant parties.	■ Given the overwhelming support for the proposal, we plan to proceed with including it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ Consideration should be given to providing expressly for the date when the service of a notice by electronic	❖ Noted. Relevant provisions will be introduced.

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	means becomes effective.	
	❖ To reduce the possibility of misunderstandings arising from slips in postal delivery or in receiving messages, it is suggested that the intended recipient may opt to receive notices or documents in hardcopy form only, in electronic form only, or concurrently in both forms.	❖ Our proposal is intended to give flexibility to a liquidator by allowing the liquidator to send documents to the intended recipients by electronic means, subject to their prior agreements and to fulfilling other conditions. If the intended recipient wishes to receive documents only in such forms as are currently allowed by the legislation, he can simply refuse to give the relevant consent to the liquidator. However, since it may not be suitable for certain documents to be sent by electronic means, despite the intended recipient's consent, the proposal should also give flexibility to the liquidator by allowing him to choose to send the documents otherwise than by electronic means. Therefore, it is not appropriate to allow the intended recipient to opt to receive documents by electronic means only. In addition, for communications and documents sent by liquidators to other relevant parties, it is possible that the recipients would be required to take actions within a certain period of time upon receipt of the communications and documents. Allowing the intended recipient to opt for adopting different means of communications concurrently may lead to confusion in computation of time limit and is therefore considered not appropriate.
	❖ It is not clear whether the definition of "other electronic means" would include or exclude the use of facsimiles in addition to emails and websites.	❖ Noted. It is the intention to allow communication by the liquidator by the use of facsimiles as well.
	❖ It is unclear as to why there are separate notification requirements for (a) the delivery of documentation by electronic means (paragraph 4.21(a) of the consultation document) and (b) the delivery of documentation through the use of websites (paragraph 4.21(b) of the consultation document). The means of giving notice pursuant to both of these subparagraphs is not specified and ought to be.	❖ A notification requirement is particularly crucial when websites are used. Otherwise, the recipient would have to check the website frequently to find out if anything has been published or sent to him via the website. Detailed provisions will be set out in the draft legislation on these requirements.

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	❖ Requiring the prior consent of a recipient to the liquidator's use of electronic means of communication may be impractical; it is also unclear what is intended by the phrase "secure the prior consent".	❖ Prior consent is essential before electronic communications could be used since electronic communications may not be accepted by all intended recipients (some of whom may not have access to the necessary equipment). Therefore, the intended recipient must have agreed, generally or specifically, that the document may be sent by electronic means of communication before such means could be used.
	❖ Provisional liquidators and liquidators should be permitted to seek the recipients' agreement to receiving communications electronically on a continuing (not only case by case) basis.	❖ Noted. Under our current proposal, the intended recipient may choose to give consent generally or specifically.
	❖ In practice, liquidators usually do not have a complete list of creditors to enable them to issue the proposed notice or circular, in particular, in the early stage of administration. Provisional liquidators and liquidators should be able to specify in the notice of appointment published in the Government Gazette and filed with the CR that it is their intention to deliver notices or documents by electronic means (e.g., using email or through websites). The notice would specify details of designated email addresses and websites for communication purpose, including the contact details which may be used to request hard copies of notices or documents.	❖ The current proposal is intended to facilitate communication by provisional liquidators and liquidators with creditors, contributories, members of COI and other interested parties by allowing provisional liquidators and liquidators to use electronic means of communication as an alternative to traditional means of communication. Yet, the prior consent of the intended recipient is considered an essential element for the use of electronic means of communications. Our proposal is not intended to be a measure for the liquidator to fulfil his duty i.e. to locate and contact all creditors in a winding-up, by publishing documents in websites unilaterally without consent.
	❖ Provisional liquidators or liquidators should provide hard copies of the notice or document upon receiving a written request from the intended recipient.	❖ Under our proposal, we will introduce provisions to allow a recipient to request the document or information in paper form.
	❖ The standard proof of debt form should be modified to allow creditors to opt to receive future correspondence from liquidators by electronic means, by providing a	❖ Under our proposal, if electronic delivery is acceptable to a recipient, the liquidator is required to obtain the consent or agreement of the intended recipient on the electronic means to be adopted and other

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	designated email address.	details. We do not propose to restrict the form of such consent or agreement.
	❖ The introduction of electronic communications should be seen as augmentation and not replacement of traditional hard copy communications.	❖ The proposal provides the liquidator with the flexibility of using electronic means of communications if the recipients agree. It does not undermine the validity of the traditional form of communication.
	❖ One-off consent is preferred. The "opt out" provisions require bolstering to be in line with other new CO requirements regarding shareholder circulars.	❖ Noted. The intended recipient is at liberty to give consent generally or specifically. Provisions modelling on relevant provisions in the new CO will be included in the draft legislation.
	❖ Personal data disclosed in a website is often difficult to control. Regard must be given as to whether public disclosure of such information (which may contain personal data) is indeed necessary. If it is considered necessary to disclose personal data on a website having regard to the circumstances, one should consider prescribing in the proposed legislation the purpose, the limitation and the sanctions on misuses of personal data.	❖ Where personal data is involved, as a data user, the provisional liquidators or liquidators are already bound by the data protection principles and other provisions set out in the PDPO. This duty of compliance applies irrespective of whether traditional or electronic form of communication is used. In case of any breach, the provisional liquidators or liquidators would be subject to the sanctions under the PDPO. The proposal is not intended to impose any obligation on, or to authorise, the provisional liquidators or liquidators to make personal data available to the public that they are not currently required or authorised to do.
	■ There was concern that many grassroot workers were not familiar with the use of electronic communication.	■ Under our proposal, the liquidator would need to obtain prior consent by the intended recipient before any notice or document could be given, delivered or sent to him by electronic means. Persons who are not familiar with the use of electronic communication may refuse to give such consent.
	<u>Chapter 5 – Voidable Transactions</u>	
A	***Introducing new provisions on "transactions at an undervalue"***	
	Question 25(a): Do you agree that new provisions should be introduced to empower the court to make orders for restoring the position of a	

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	company to what it would have been if the company has not entered into a transaction at an undervalue?	
	■ An overwhelming majority of respondents supported introducing provisions to empower the court to make orders in relation to a company which has entered into a transaction at an undervalue.	■ We welcome the positive feedback and will proceed to include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The provisions should be drafted in such a manner so as to ensure that, as the UK case law confirms, the creation of security over a company's assets does not constitute a transaction at an undervalue. Separately, the manner in which consideration received and provided by the company should be assessed in money or money's worth as in the UK legislation.	❖ Our intention is to model the new provisions on those in the UK and in the BO. The definition of "transaction at an undervalue" will be drafted with reference to those provisions. An express provision would be included to provide that the value of the consideration is to be assessed "in money or money's worth".
	❖ Besides an order for restoring the position before the transaction, alternate remedies should be available e.g. an order for vesting the proceeds of sale of relevant property or requiring any person to pay, in respect of benefits received by him from the company, such sums to the liquidators as the court may direct.	❖ Under the current proposal, on finding that a transaction at an undervalue has been entered into, the court will have a wide discretion to make an appropriate order. The court's general power is supplemented by a list of specific orders similar to the list set out in section 51A of the BO. The types of order suggested by the respondent are covered by the list.
	Question 25(b): Do you agree to the proposal that the "relevant time" should be any time within the period of five years ending with the commencement of the winding-up?	
	■ A majority of respondents agreed that the "relevant time" should be any time within the period of five years ending with the commencement of the winding-up.	■ We welcome the positive feedback and will proceed to include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ Some respondents suggested following the UK and Australian legislation which provide for a look-back	❖ While some respondents asked for a longer or a shorter look-back period, the proposal for a five-year look-back period is in line with that

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	period of two years since a long look-back period brings greater uncertainty to commercial arrangements as it increases the risk of invalidation by the courts. On the other hand, a respondent proposed that there should be no time limit for a liquidator to seek for recovery from a transaction at an undervalue.	for bankruptcy cases under the BO in Hong Kong and the recommendation of the Law Reform Commission, and is considered appropriate by the majority of respondents during the consultation. It should be noted that a transaction will only be caught by the provision if at that time the company was unable to pay its debts or became unable to pay its debts as a result of the transaction and the value of the consideration received by the company is 'significantly' less than the value of the consideration provided by the company.
	❖ The definition of "relevant time" ought to distinguish between persons connected with the company (say two years) and those persons who are not connected with the company in which case a shorter time frame should apply (say six months).	❖ Our proposal already makes a distinction between "persons connected with the company" and those who are not connected. Under our proposal, when a company enters into a transaction at an undervalue with "persons connected with the company", it is presumed that the company was unable to pay its debts at that time of the transaction or became unable to pay its debts as a result of the transaction, since such persons are in a position to take action to manipulate or exert influence on the affairs of the company in order to safeguard or gain some advantage for their own interests. There is no such presumption of insolvency for persons who are not connected with the company and we consider that this arrangement is more appropriate.
	Question 25(c): Do you agree that transactions at an undervalue entered into by the company with a person who is connected with the company should be subject to more stringent control as proposed in paragraph 5.11?	
	■ An overwhelming majority of respondents agreed that a person who is connected with the company should be subject to more stringent control.	■ We welcome the positive feedback and will proceed to include the proposal in the draft legislation.
	■ A respondent would like to clarify whether the proposal was intended to adopt the relevant position under the BO, such that (a) the proposal would catch all transactions which took place within 2 years of the commencement of	■ To clarify, we would not adopt the relevant provision of the BO which has the effect of catching all transactions at an undervalue that took place within two years of the commencement of the liquidation irrespective of the solvency status of the company. Under our proposal, the

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	the winding-up, but (b) where the transaction took place more than 2 years before but within 5 years of the commencement of the winding-up, the provision would only bite if it could be shown that the company was either insolvent at the time of the transaction or became insolvent in consequence of that transaction.	transactions at an undervalue which took place during the five-year look-back period would only be caught if the company was unable to pay its debts at the time of the transaction or became unable to pay its debts as a result of the transaction.
	■ There were respondents who considered the adoption of the statutory presumption of insolvency for persons who are "connected with the company" might capture a company's bank/major supplier. It was considered that this will have a negative impact on banks' incentives to render assistance to companies in financial difficulties, and will also bring uncertainty to ordinary business dealings for major suppliers. Therefore, it was suggested that banks and major suppliers should be excluded from the definition of "persons connected with the company".	■ Under our proposal, a statutory protection is provided such that genuine business transactions, i.e. transactions carried out in good faith and for the purpose of carrying on the company's business and that at the time of the transaction there were reasonable grounds for believing that the transaction will benefit the company are protected. The reasons for specifically excluding banks and major suppliers in the definition of "persons connected with the company" are not clear.
	Question 25(d): Do you agree that statutory protection should be provided for the party seeking to resist an application made by the liquidator of a company in respect of the undervalue transaction? If so, do you agree with the statutory protection as proposed in paragraph 5.12?	
	■ An overwhelming majority of respondents agreed that statutory protection should be provided for the party seeking to resist an application made by the liquidator of a company in respect of the undervalue transaction.	■ We welcome the positive feedback and will proceed to include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The onus should be on the person who resists the order to prove the requirements of the defence being fulfilled. In relation to the transaction made by directors, the directors should have exercised due consideration and should have board resolutions and valuation report, etc.	❖ While the liquidator bears the burden of establishing a case for transaction at an undervalue, the onus of establishing a defence should be on the respondent to the claim. The proposal is not intended to catch genuine business transactions carried out in good faith. Whether a transaction is a genuine business transaction or not could be

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	to demonstrate that the directors entered into the transaction in good faith and for the benefit of the company.	established by contemporaneous records or by other means.
	❖ With regard to the definition of 'the purpose of carrying on its business', it would be useful to make reference to similar legislation in Australia.	❖ We have considered both the UK and the Australian legislation. As the existing voidable transactions provisions in the C(WUMP)O and the BO were based on the relevant provisions in the UK, modelling the new undervalue transaction provisions on the corresponding provision in the UK, which has a long history with the support of case law, would be more consistent with the existing provisions. On the other hand, the legal framework for voidable transactions in Australia is quite different from that in Hong Kong or in the UK.
	❖ It is difficult to define any strict statutory protection as it would vary from case to case. It seems that the "recipient" of the undervalued asset may not be able to deploy the defence as currently proposed if it concerns the operation of the business of the company.	❖ The proposed statutory defence provision was modelled on the relevant provision in the UK, and represents an appropriate balance between the need to impeach improper transactions for the benefit of creditors in a winding-up and the need to allow room for genuine business transactions which are conducted in good faith to enhance the chance of survival of the distressed companies. The protection offered by the defence is not limited to directors and may be invoked by third parties as well.
B	***Rectifying the anomalies in the application of existing provisions on "unfair preference"***	
	Question 26(a): Do you agree that the current provisions in the C(WUMP)O incorporating the provisions in the BO on unfair preferences should be replaced by new standalone provisions which apply to winding-up cases to rectify the existing anomalies which limit the application and effectiveness of such provisions?	
	■ An overwhelming majority of respondents supported the proposal to provide new standalone provisions which apply to winding-up cases on unfair preferences.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include-	

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	❖ There are occasions when a company is failing that insurance companies will continue to cover sales in return for getting some payments from the buyer. Those payments should not be subject to voidable preference.	❖ Our proposal aims at introducing a self-contained set of unfair preference provisions in the C(WUMP)O, and we have not proposed any change to the existing legal position in which the unfair preference provisions in the BO are applied in the company winding-up context.
	❖ The format of sections 239 and 240 of the UK Insolvency Act 1986 should be adopted to distinguish the treatment of those persons connected with the company and those who are not.	❖ We will make reference to sections 239 and 240 of the UK Insolvency Act 1986 when preparing the draft legislation.
	❖ The relevant time with respect to an "associate" case should be five years, being the same as that for a transaction at an undervalue.	❖ The majority of respondents supported maintaining the two-year period of "relevant time" for unfair preference. We do not see a clear case for extending this period.
	❖ The issue regarding section 50(4) of the BO, whereby the company must evidence that it was "influenced by a desire to prefer" is not addressed. This limb will continue to be a significant barrier for liquidators pursuing unfair preference claims.	❖ Our proposal aims at introducing a new standalone set of provisions in the C(WUMP)O on unfair preference which would largely follow the existing provisions in the BO and maintaining the present position of the law. There is no clear case for altering the existing legal position.
	Question 26(b): Do you agree with the definitions of "person who is connected with a company" and "associate" as proposed in paragraphs 5.19 and 5.20 of the consultation document?	
	■ A majority of respondents supported the definitions of "person who is connected with a company" and "associate" in the consultation document.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The drafting of the legislation should make it clear that "major shareholders" and "controlling shareholder" should be considered to be "a person who is connected with the company".	❖ Under our proposal, the definition of "a person who is connected with the company" would be able to cover the concepts of "major shareholders" and "controlling shareholder".

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	❖ It is further suggested that a person is an associate of an individual if that person is accustomed to act in accordance with the individual's directions or instructions.	❖ Under the current proposal, "a person who is connected with the company" already includes a shadow director of the company, and a shadow director means a person in accordance with whose directions or instructions (excluding advice given in a professional capacity) the directors, or a majority of the directors, of the company are accustomed to act.
	❖ In the Listing Rules, the threshold is 30%. There is a good reason or need to make the threshold consistent across different laws and rules.	❖ Noted. Instead of adopting the requirement of "one-third or more of the voting power" for determining "control of a company" in the definition of "associate", the requirement of "more than 30% of the voting power" will be adopted. The threshold of "control" would then be aligned with relevant provisions in the new CO and the Listing Rules.
	❖ Each category of associate should be sign-posted in the manner adopted in section 435 of the UK Insolvency Act 1986.	❖ The Law Draftsman would consider how best to draft the provision in accordance with the prevailing drafting convention.
	❖ The proposed definition of "associate" seems to have missed out holding companies whose shares are not owned in the name of the person who is connected with the debtor company or an associate of such person.	❖ Paragraph 5.20(f) of the consultation document covered holding companies. A holding company of the debtor company would be regarded as an associate of the debtor company as it would hold a voting power of the debtor company above the statutory threshold.
	■ There were respondents who disagreed with the proposal as the definition of "person who is connected with the company" may inadvertently capture a company's bank or major supplier.	■ Whether a person is considered as "connected with the company" would depend on the facts of the case and the substance of the relationship of the bank or the major supplier with the company. There is no clear reason for excluding banks and major suppliers in the definition of "persons connected with the company" .
	Question 26(c): Do you agree that the existing protection for persons who have received benefits or acquired or derived any interest in property in good faith and for value from unfair preference should be maintained, and also be applicable to the proposed new provisions on transactions at an undervalue?	

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	■ An overwhelming majority of respondents supported the proposal to maintain the existing protection provisions on unfair preference, and also apply the same protection provisions on transactions at an undervalue.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ In relation to the transaction made by directors, the directors should have exercised due consideration and should have board resolutions and valuation report, etc. to demonstrate that the directors entered into this transaction in good faith and for the benefit of the company.	❖ The issue of whether a person receives benefits or acquired or derived interest in property in good faith and for value is to be decided on a case-by-case basis, having regard to the facts of the case, available evidence, etc.
C	***Improving the effectiveness and flexibility of the provision for invalidating floating charges created before the winding-up of the company***	
	Question 27: Do you agree to the proposed special provisions in relation to floating charges created by a company in favour of a person who is connected with the company?	
	■ All respondents supported the proposal for special provisions in relation to floating charges created by a company in favour of a person who is connected with the company.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ There were respondents who suggested that a provision along the lines of section 245(2)(b) of the UK Insolvency Act should be introduced, to the effect that the value of consideration which consists of the discharge or reduction, after, the creation of a charge, of any debt of a company, should not be treated as invalid as this does not discriminate against other creditors in the future.	■ Section 267 of the C(WUMP)O is designed to avoid any floating charge created shortly before liquidation which merely results in converting unsecured creditors into secured creditors, and thus which brings no new value to the company. In considering these cases, the court will look at the substance of the transaction and determine whether any new value is genuinely and in substance given by the holder of the floating charge to the company. We will not adopt the proposed UK provision since the proposed UK provision may allow the creation of a floating charge with consideration consisting merely of the discharge or reduction of an

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		existing debt owed to the floating chargee which does not bring new value.
	Question 28: Do you support the expansion of the scope of the exemption of a floating charge from invalidation catered for genuine credit transactions to cover "property and services supplied to the company" and "money paid at the direction of the company"?	
	■ A majority of respondents supported the proposal to expand the scope of the exemption of a floating charge from invalidation catered for genuine credit transactions to cover "property and services supplied to the company" and "money paid at the direction of the company".	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ There are uncertainties in relation to the expansion of the scope of the exemption, which may lead to issues, disputes and/or litigations. The scope of the exemption in the present legislation, namely "the amount of any cash paid to the company", is clearer and more certain.	❖ The suggested amendment would cover credit arrangements which involve the supply of property or services on credit. It would allow greater commercial flexibility between credit providers and the consumer companies in relation to commercial transactions. This proposal is modelled on the relevant provisions in the UK.
	❖ The issue of valuation in the case of property and services supplied to the company should be addressed. It may not be a straightforward exercise to assess the genuine value of an asset or service. A variation of section 245(6) of the UK Insolvency Act 1986 which attempts to provide a definition of the value of goods and services should be adopted.	❖ To clarify, in preparing the draft legislation, we will make reference to the relevant UK provisions as suggested by the respondents in relation to how the value of goods and services is to be determined.
	❖ Some respondents suggested that some other typical forms of valuable consideration (the transfer of land or shares) which arise from day-to-day trading and finance should be included. A few respondents also suggested that the scope of the exemption of a floating charge	❖ Section 3 of the Interpretation and General Clauses Ordinance (Chapter 1) provides that property includes money, goods, choses in action and land (and obligations, easements and every description of estate, interest and profit, present or future, vested or contingent, arising out of or incident to such property).

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	from invalidation catered for genuine credit transactions to cover property (especially intangible assets) and services supplied to the company should be clearly stipulated. ❖ The expansion of the scope should include "new money" for working capital facilities as the company can benefit from the sales generated by the working capital facilities and pay off its debts.	❖ The proposal is not intended to catch genuine credit transactions which create floating charges to secure new value to a company. Therefore, to ensure that such genuine credit transactions are not affected by the invalidation provisions, it is presently provided that a floating charge is not invalid to the extent of "the amount of any cash paid to the company" at the time of or subsequently to the creation of the floating charge and in consideration of the floating charge. The amendment to replace "cash paid to the company" with "money paid to or at the direction of the company" will not alter this position.
	■ Some respondents disagreed with the proposal with the following reasons – ❖ Floating charge created in good faith should be validated. ❖ The proposal may pose difficulty for the liquidators to obtain documents to verify the fund flow between the connected person and the credit providers and trade creditors.	❖ A floating charge created in good faith may also have a potentially adverse effect on other unsecured creditors in the winding-up process. We do not consider that there is a clear case to change the present legal position, which is in line with that in the UK and Australia. ❖ The liquidator is given wide powers to investigate into the affairs of the company being wound up. If necessary, the liquidator may seek assistance from the court e.g. under section 221 of the C(WUMP)O to invoke a private examination.
	<u>Chapter 6 – Investigation during Winding-up, Offences Antecedent to or in the Course of Winding-up and Powers of the Court</u>	
A	***Enhancing the effectiveness of the private and public examination procedures by providing for the express abrogation of the privilege against self-incrimination***	
	Question 29(a): Do you agree to expressly set out in the legislation the common law position that a person summoned for either a private or a	

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	public examination cannot invoke the privilege against self-incrimination during the examination? *Question 29(b): If so, do you agree that we should introduce provisions to prohibit the subsequent use of answers given and statements made during the examination in subsequent criminal proceedings if certain conditions are satisfied, subject to certain exceptions such as offences relating to perjury and provision of false statement and offences under the C(WUMP)O?*	
	■ An overwhelming majority of respondents supported expressly setting out in the legislation the position under case law that a person summoned for either a private or a public examination cannot invoke the privilege against self-incrimination during the examination. They also agreed that provisions should be introduced to prohibit the subsequent use of answers given and statements made during the examination in criminal proceedings subject to certain exceptions.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ It is common that section 221 is invoked to require provision of documents. The legislation should expressly provide whether or to what extent the respondent can claim legal professional privilege.	❖ Legal professional privilege has been claimed in the context of production of documents under section 221 in a number of decided cases. We have no intention to alter this common law position.
	❖ It is not clear from the proposal that if the "certain conditions" being referred to, for the answers given or statements made by the person not admissible as evidence in subsequent criminal proceedings, are limited to "the answer or statement might tend to incriminate him and that he so claims before giving the answer or making the statement at either examination".	❖ The "certain conditions" as stated in the consultation document are that "the answer or statement might tend to incriminate him and that he so claims before giving the answer or making the statement at either examination".
	❖ As to the proposal that the prohibition will be subject to "certain exceptions", it is not clear if the exceptions are to be limited to the examples given, i.e. the person is	❖ Under our current proposals, if a person is required to give an answer to a question or make a statement pursuant to section 221 or 222 of the

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	charged with offences relating to (1) perjury, (2) provision of false statements or (3) other offences under the C(WUMP)O.	C(WUMP)O and the answer and the statement might tend to incriminate the person and he has so claimed before giving the answer or making the statement, the requirement, question and answer , and statement will not be admissible in evidence against him in criminal proceedings in a court of law, other than those in which he is charged with perjury or an offence or an offence under Part V of the Crimes Ordinance or section 349 under the C(WUMP)O in respect of the answer or statement.
	❖ A person must not be lightly deprived of the privilege against self-incrimination unless there are compelling justifications. Besides, it should be considered whether the public interest in ensuring that effective and efficient liquidation investigation is so compelling to justify the proposal.	❖ As recognised by the case law, the purpose of examinations under sections 221 and 222 is to trace and secure the assets of the company for the benefit of the creditors and the contributories where the assets are missing and the documentation does not adequately explain their whereabouts. Such legislative purpose would be frustrated if the privilege against self-incrimination is not abrogated. Our proposal is intended to expressly abrogate the privilege against self-incrimination so that the purpose of the legislation would not be defeated, and at the same time to give the examinee an express statutory protection in criminal proceedings against him subject to certain criteria and exceptions.
B	***Widening the scope of application of the public examination procedure***	
	Question 30(a): Do you agree to the removal of the requirement that the OR or the liquidator must have alleged in his "further report" that fraud has been committed for initiating the public examination procedure, and to provide that a public examination may be ordered by the court upon the application by either the liquidator or the OR? *Question 30(b): Do you agree with the proposed new categories of person that may be examined under the public examination procedure, namely (i) any person who has acted as liquidator of the company or receiver or receiver and manager of the property of the company; and (ii) any person who is or has been concerned, or has taken part, in the management of the company?*	
	■ An overwhelming majority of respondents supported removing the requirement that the OR or the liquidator	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.

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	must have alleged in his "further report" that fraud has been committed for initiating the public examination procedure. They also agreed with the proposed new categories of person that may be examined under the public examination procedure.	
	■ Other comments raised by individual respondents include- ❖ The proposal appears to facilitate "fishing" by liquidators without requiring them to properly turn their minds to why they might have grounds to proceed with a public examination rather than to invoke the private examination procedure.	❖ Our proposal will not change the present legal position that the court's approval is required for conducting either a public examination or a private examination, and that the applicant would need to satisfy the court that there is a need for conducting the examination.
	❖ The categories of person that may be summoned for a public examination should be extended to cover associates and connected persons.	❖ The purpose of this proposal is to facilitate the investigation by the liquidator into the affairs of the company and the persons involved in the conduct of its affairs. Therefore, it is appropriate to confine the categories of person that may be summoned to any person who is or has been an officer of the company, any person who is or has been concerned or has taken part in the promotion or formation or management of the company, and any past liquidator, provisional liquidator or receiver or manager of the company.
	❖ By section 204 of the C(WUMP)O, the OR has control over liquidators and can require any liquidator to answer any inquiry in relation to any winding-up in which he is engaged. As such, it is not necessary to obtain information from the liquidators / receiver / receiver and manager by way of public examination.	❖ Section 204 of the C(WUMP)O relates to the OR's control over liquidators and provides that the OR may inquire into the case "where a liquidator does not faithfully perform his duties or duly observe all the requirements imposed on him by statutes, rules or otherwise with respect to the performance of his duties". Under our current proposal, the OR may apply to the court for examining the liquidator, amongst other persons, under section 221 on the affairs of the company and a person's conduct and dealings in relation to the company. The scope of the two sections is not entirely the same.
	■ A few respondents did not agree with the proposal (or	

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	certain aspects of the proposal), and the reason given are as follows- ❖ the proposed removal of the section 222(1) requirement to make a further report alleging fraud so as to invoke the public examination process is not justified.	❖ Under the present law, in order to invoke the public examination procedure, the court has to be satisfied on the need for invoking the procedure having regard to the circumstances of the case. As a public examination will enable the creditors and the community at large to have the chance to know the salient facts and unusual features connected with the company's failure, the court should not be restricted to allowing public examination only when there is an allegation of fraud. There is no such restriction in the public examination procedure in the BO nor in the relevant provisions in the UK legislation.
	❖ There was not any justification given for adding further categories of persons that might be summoned to attend before the court for a public examination. Any person who has acted as liquidator of the company or receiver or receiver and manager of the property of the company should not be subject to public examination as all the information and documents of the company acquired by them under their appointment should have been properly recorded and kept during the administration by them which can be made available upon request pursuant to section 201 of the C(WUMP)O. The rationale behind public examination was to permit a liquidator to ascertain the truth about the affairs of a company as expeditiously and economically as possible.	❖ The justifications for including additional categories of persons that might be summoned to attend before the court for a public examination were clearly set out in paragraph 6.16 of the consultation document. In particular, the proposal to provide that a liquidator, a receiver or a receiver and manager could be subject to the public examination procedure would enable the procedure to be invoked to obtain information from such persons for the purpose of investigating the liquidation process itself where necessary. Such information may not be properly recorded or kept in the books and records which are required to be kept under section 201 of the C(WUMP)O. The proposal to include additional categories of persons that might be summoned to attend before the court for a public examination is in line with the relevant provision in the UK.
C	***Providing for liability of past directors and members in connection with a redemption or buy-back of shares out of capital***	

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	Question 31(a): Do you agree that if a company is wound up insolvent within one year of its shares being redeemed or bought back by payment out of capital, the recipients of the payment of the redeemed or bought-back shares and the directors making the solvency statement in respect of the redemption or bought-back shares without having reasonable grounds for the opinion expressed in the statement should be required to contribute to the assets of the company for an amount not exceeding the payment made by the company in respect of the shares redeemed or bought back by the company so as to meet the deficiency in the company's assets? *Question 31(b): If so, should the members from whom the shares were redeemed or bought back and the directors who made the solvency statement which supported the redemption or buy-back without having reasonable grounds for the opinion expressed in the statement be jointly and severally liable to contribute to such assets?*	
	■ An overwhelming majority of respondents agreed in principle with the proposal that if a company is wound up insolvent within one year of its shares being redeemed or bought back by payment out of capital, the recipients of the payment of the redeemed or bought-back shares and the directors who made the solvency statement in respect of the redemption or bought-back shares without reasonable grounds for the opinion expressed in the statement should be jointly and severally liable for an amount not exceeding the payment made by the company in respect of the shares redeemed or bought back by the company so as to meet the deficiency in the company's assets.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The category of persons who ought to make a contribution to the assets of the company in the manner provided for in the proposal should be limited to those persons who are connected with the company. It should only be those closest to the company who ought to be held accountable. Or a distinction should be drawn between persons who are connected with the	❖ As the rationale of the proposal is to protect the interests of creditors by ensuring that the company's paid-up capital is preserved and not returned to its members shortly before the insolvent winding-up of the company, it is reasonable and appropriate to apply the proposal to listed and unlisted companies uniformly, and also equally to all types of persons who are recipients of the payment of the redeemed or bought-back shares.

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	company and those who are not so connected. As currently drafted this provision is open to innocent parties being caught by the provision (e.g. retail investors). The proposal should only apply to substantial shareholders as defined under the SFO for public companies.	
	❖ There would be practical difficulties in tracing the members from whom the shares were redeemed or bought back in the case of public companies, in particular, listed companies. Besides, it would not be practical to recover the money from retail investors or make them jointly and severally liable for the amount that they have received For listed companies, the amount of payment involved in the buy-back of shares is enormous, and some company directors may not be able to bear that. There will also be difficulties in actual enforcement.	❖ Under the new CO, a listed company is forbidden from buying back its shares out of capital on an approved stock exchange. Therefore, a listed company may only buy back its shares out of capital under a general offer or through a contract authorised in advance by special resolution. As the shareholders from whom the shares are bought back should be clearly identified in these situations, concerns about the practical difficulties in tracing the members from whom the shares were brought back by listed companies should not arise.
	❖ For private companies, the relevant period should be extended from within one year to within two years of the shares being redeemed or bought back by payment out of capital. The proposed two-year period is in line with the relevant time for unfair preference.	❖ The proposed one-year period is in line with the requirement of the solvency test and a solvency statement under sections 205 and 206 of the new CO, which is required to support a payment out of capital under section 259 of the new CO.
	❖ The proposal should only catch the recipient of the payment of the redeemed shares. If the directors are to be held liable under the proposal, the directors may use a lot of resources to verify the circumstances of the	❖ Directors are protected under our proposal as a director would only be held liable if he made the solvency statement supporting the redemption or buy-back without having reasonable grounds for the opinion expressed in the statement. In fact, section 207 of the new

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	company before signing documents and this will add to the operation cost of the company. Some directors may refuse to sign relevant documents in order to avoid liability, this will bring negative effect to the operation of the company.	CO already provides that it is an offence for a director to make a solvency statement without having reasonable grounds for the opinion expressed in it.
	❖ The definition of "members", "recipient" and "directors" should cover corporate shareholders and corporate directors (incorporated in Hong Kong or overseas) all the way to the ultimate natural persons who own and control these legal entities.	❖ Noted. Under our proposal, liabilities to repay are imposed on the legal owners of the shares (whether an individual or a body corporate) since only the legal owners are entitled to receive the payment. Liabilities to repay are also imposed on the directors (whether an individual or a body corporate) making the solvency statement in respect of the redemption or bought-back shares without having reasonable grounds for the opinion expressed in the statement. In preparing the draft legislation, we will also provide that a person who has contributed any amount to the assets may apply to the court for an order directing any other person jointly and severally liable in respect of the payment.
	Question 31(c): Should the members and the directors concerned be allowed to apply for winding-up of the company on grounds that the company is unable to pay debts or that the court is of opinion that it is just and equitable that the company should be wound up (but not on other grounds)?	
	■ An overwhelming majority of respondents supported that the members and the directors concerned in respect of the bought-back shares should be allowed to petition for winding-up of the company.	■ We are pleased to note the respondents' support for this proposal and will include it in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ There is a British Virgin Islands case that a holder of preference shares who has issued a redemption notice may not petition based on the redemption proceeds. This position is sensible and should be adopted in Hong Kong.	❖ It appears that the said case concerns the right of a shareholder, as creditor, to petition in relation to the outstanding sum to be paid by the company in respect of the redemption (i.e. a debt owed to the member in the position as member). Instead, our proposal concerns the right of the concerned persons, who are contributories as a result of the new

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		liability to contribute to the asset of the company in its insolvent winding up, to petition. Thus, the contexts are different and are not comparable.
	■ It is unclear whether such persons should be allowed to apply for winding-up of the company. The proposal would limit the amount of liability of the members and/or directors to "an amount not exceeding so much of the relevant payment as was made by the company in respect of the shares redeemed or bought back". On this basis, the members and/or directors would only be liable for that amount of capital that had been authorised to be paid out to them. There would not necessarily be any concern on their part regarding additional losses or depletion of assets which are not attributable to the redemption or buy back of the relevant shares.	■ Similar to the case of other contributories (e.g. holders of partly paid shares), the liabilities of a person to contribute under the proposed provision is limited to a certain sum. However, this should not affect their right to present a petition.
	<u>Other Technical Amendments (Annex C of the consultation document)</u>	
2	***To extend the time limit in which a company is required to give notice of a resolution for voluntary winding-up by advertisement in the Gazette to 15 days, instead of 14 days, after the passing of the resolution***	
	■ All respondents supported this technical proposal, with a comment raised by an individual respondent- ❖ The time limit for giving notice of a voluntary winding-up resolution should be further extended to 21 days to allow time in case there are public holidays within the notice period.	■ We will proceed with including the proposal in the draft legislation. ❖ The resolution for voluntary winding-up of a company is a piece of important information to the stakeholders of the company and should be published in the gazette as soon as possible. We consider that a period of 15 days should be sufficient to address any issue arising from intervening public holidays and we do not consider it appropriate to further extend the notice period to 21 days.
3	***To set out the obligations of the liquidator in a members' voluntary winding-up where he is of the opinion that the company will not be***	

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	able to pay its debts in full within the period stated in the certificate of solvency issued under section 233 of the C(WUMP)O	
	■ An overwhelming majority of respondents agreed to this technical proposal, with comments raised by individual respondents-	■ We will proceed with including the proposal in the draft legislation.
	❖ The minimum notice period for calling the first creditors' meeting should be ten days instead of seven days.	❖ As in the case of a creditors voluntary winding-up, we consider that a minimum notice period of seven days for calling the creditors' meeting is appropriate. There are similar requirements of minimum length of notice in the UK and Australian legislation for the first creditors' meeting.
	❖ Regarding the proposal that the liquidator should provide creditors with all reasonable information concerning the affairs of the company free of charge, it requires clarity as to what is "reasonable information", "free of charge"; i.e. not chargeable to the creditors but chargeable against the estate.	❖ This proposal is modelled on the UK legislation. The liquidator would be required to furnish such information concerning the affairs of the company as the creditors may reasonably require in the circumstances of each case. Under the C(WUMP)O, costs, charges and expenses properly incurred in a voluntary winding-up are payable out of the company's assets.
	❖ A note should be included in the notice of the creditors' meeting setting out the reasons for believing a conversion from a members' voluntary winding-up to a creditors' voluntary winding-up is necessary. Consideration could be given to providing a template report showing the relevant information to be provided to the creditors.	❖ The reason for a liquidator to summon a meeting under section 237A of the C(WUMP)O is that the liquidator is of the opinion that the company will not be able to pay its debts in full as stated in the certificate of solvency. Under our proposal, a liquidator is required to lay before the creditors' meeting a statement of affairs of the company in which the relevant information such as the assets, debts and liabilities of the company would be set out. Such information would enable creditors to appreciate the financial status of the company. Instead of adopting a template report, we plan to specify such information in the form of a list in the proposed legislation.
	❖ Under the scenario as described in this technical proposal, similar meeting arrangements as for a creditors' voluntary winding-up should be adopted.	❖ Under our present proposal, the proposed meeting arrangements are largely in line with those applicable to a creditors' meeting in a creditors' voluntary winding-up. Modifications are however

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		necessary to cater for the fact that this is a conversion case.
6(a)	***To prescribe the resignation procedure for a liquidator appointed in a voluntary winding-up***	
	■ An overwhelming majority of respondents supported this technical proposal.	■ We will proceed to include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The procedures set out in rule 154 of the CWUR are not limited to a court winding-up. There is case law showing that rule 154 is also applicable in a creditors' voluntary winding-up. ❖ CR apparently has problems dealing with filing of notices of resignation of some of the joint liquidators in the course of liquidation.	❖ It is expressly stipulated in rule 153(4) of the CWUR that rule 154 shall apply only in a court winding-up. It is therefore necessary to make a provision to prescribe the resignation procedure for a liquidator appointed in a voluntary winding-up. ❖ At present, a liquidator resigning from his appointment in a voluntary winding-up case is required to file a notice of cessation to act as liquidator in the specified form (Form NW5 or previously Form W5). In cases involving joint liquidators, the notes for completion of Form NW5/W5 have already made it clear that "separate forms should be used to notify the Registrar". The practice of filing of notices of cessation to act as liquidator (Form W5/NW5) has been working well and there are no problems in the filing of the notices.
6(b)	***To provide that a liquidator in a creditors' voluntary winding-up may be removed by a creditors' meeting specially convened for the purpose***	
	■ An overwhelming majority of respondents supported this technical proposal.	■ We will proceed to include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The liquidator to be removed should have the opportunity to make representations for himself in writing in advance of the creditors' meeting to be circulated to all creditors, similar to the mechanism for	❖ The proposal on the power of creditors to remove a liquidator in a creditors' voluntary winding up is similar to the provision on the power of a company to remove a liquidator in a member's voluntary winding up under section 235A of C(WUMP)O, which does not

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	the removal of directors. If there is any disagreement to the resolution for the removal of liquidators, an application can be made to the court to review the decision within a reasonable timeframe, say within 21 days from the date of the meeting of creditors.	provide for a liquidator to have the right to make representations before the creditors' meeting in order to preserve the simplicity of the proceedings.
6(d)	***To add that application to court under section 205 of the C(WUMP)O for release may also be made in the case where the liquidator ceases to hold office due to his death or becoming disqualified to act***	
	■ An overwhelming majority of respondents supported this technical proposal.	■ We will proceed to include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ In the event that the liquidator cannot make an application for a release by himself (e.g. due to his death and his mental incapacity), detailed procedures should be provided as to whom should make the application on his behalf and how such an application should be made.	❖ Our proposal will provide that in case a liquidator has died, the personal representative may make an application on his behalf for the release. In case a liquidator becomes mentally incapacitated, the court may authorise a person to conduct any legal proceedings relaing to his affairs on his behalf under the Mental Health Ordinance (Chapter 136).
8	***To provide that a body corporate may be a COI member. However, a body corporate may not act as a representative of a member***	
	■ All respondents agreed to this technical proposal, with a comment raised by an individual respondent as follows- ❖ The proposal should also apply to members if the members are themselves corporations.	■ We will proceed with including the proposal in the draft legislation. ❖ Our proposal is that a body corporate cannot act as a representative of a member. In other words, the representative must be a natural person. This will also mean that a body corporate cannot act as a representative of a member who is itself a corporation.
10	***To provide that the COI members should be entitled to their reasonable travelling expenses to and from meetings of the COI within Hong Kong payable out of the company's assets***	

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	■ All respondents agreed to this technical proposal, with comments raised by individual respondents as follows- ❖ Where in case the assets of the company are not sufficient to cover the travelling expenses of the COI members, it should be stipulated in rule 179 of CWUR in respect of the priority of the repayment. ❖ The "reasonableness" of the travelling expenses should be determined by the liquidators, and should not be subject to taxation by the court.	■ We will proceed with including the proposal in the draft legislation. ❖ Under our proposal, rule 179(1) of CWUR will be amended so that reasonable travelling expense incurred by the COI members and allowed by the liquidator under the proposed provision would be given a priority. ❖ The proposed provision imposes upon the liquidator a duty to defray "reasonable" travelling expenses of members of COI as part of the expenses of a court winding-up . As in other instances, in a court winding-up, the liquidator's decision is always subject to the supervision of the court.
13	***To modernise the drafting of section 265 of the C(WUMP)O concerning the preferential status being accorded to different classes of creditors in the distribution of realised assets of a company being wound up***	
	■ An overwhelming majority of respondents supported this technical proposal.	■ We will proceed to include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ Section 265 should be redrafted and simplified in order to make the preferential provisions understandable. The status of the Employees Compensation Assistance Fund as a preferential creditor section 265(1)(ea) should be reconsidered. Consumers should be granted the status as preferential creditors for those who have made prepayment for goods and services to a company. Section 265(5B) should be extended to empower the court to allow prospective applications, and so enable	❖ The objective of this technical proposal is to modernise the drafting of this section such that it could be presented in a more user-friendly manner and a more comprehensible style. We have no plan to introduce any substantial change to this section. Any substantial change on section 265 of the C(WUMP)O will affect the interests of creditors in a winding-up, this would require in-depth discussion with stakeholders and extensive consultation. It should be taken forward under a separate due process and will not be pursued in the present exercise.

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	creditors to consider whether to fund a liquidator, taking into consideration the potential benefits.	
15	***To provide that the provisional liquidator or the liquidator may require any person who is obliged to submit a statement of affairs to submit a statement of concurrence instead***	
	■ An overwhelming majority of respondents supported this technical proposal.	■ We will proceed to include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ The proposal might encourage parties to install "dummy" directors who are not actually the persons responsible for the affairs of the company, and yet who are put forward as the main party to which queries are referred. This would potentially hinder the true protagonists from being discovered or being required to give proper particulars in their own statements. Requiring a statement of affairs from each individual requires each person to consider his or her answers specifically and individually and for them to take responsibility for such answers. The law should be clear about who will have the "primary obligation" to prepare the statement of affairs for others to concur or disagree with.	❖ Under our proposal, the choice of whether to request an affidavit of concurrence is on the liquidator. Our proposal will not change the current legal position for statement of affairs to be made out and verified by one or more of the directors and the secretary of the company under section 190 of the C(WUMP)O or by persons as listed in section 190(2)(a) to (d) as the liquidator may require. Our proposal will offer flexibility to the liquidator to require the said person to submit an affidavit of concurrence instead if the liquidator considers it appropriate to do so.
	❖ There may be concern that directors would tend to simply sign a statement of concurrence regardless of the contents of the statement of affairs they concur with. The statement of concurrence should be sworn as an affidavit, as with a statement of affairs, so that similar sanctions would apply in the case of dishonest	❖ Noted. In order to address the concern that a person signing a "statement of concurrence" may tend to give concurrence regardless of the content of the statement of affairs he concurs with, we will replace "statement of concurrence" with an "affidavit of concurrence".

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	statements. ❖ Clarification is requested on whether the provisional liquidator or the liquidator is expected to comment on the statement of concurrence, in the same manner as a statement of affairs.	❖ Similar to the case of a statement of affairs, the affidavit of concurrence is to be submitted to the provisional liquidator or liquidator, and the person who has submitted the statement of affairs or affidavit of concurrence (as the case may be) must give such further information as may be required by the OR, provisional liquidator or liquidator.
18	***To provide that an application under section 221 of the C(WUMP)O may only be made by the liquidator, and in case of a court winding-up, also by the OR***	
	■ An overwhelming majority of respondents supported this technical proposal.	■ We will proceed to include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ It is not appropriate to widen the scope of the eligible applicants to include the creditors or contributories. ❖ The section 221 powers should be extended to provisional liquidators as they may wish to obtain information for the purpose of asset tracing which would be for the benefit of creditors and contributories.	❖ Our proposal does not allow for this. ❖ Noted. We will include the provisional liquidators as an eligible party to invoke the section 221 power under our proposal.
20	***To expressly provide that the person summoned for either a private examination or a public examination may at his own expense employ a solicitor with or without counsel.***	
	■ An overwhelming majority of respondents supported this technical proposal.	■ We will proceed to include the proposal in the draft legislation.
	■ Other comment raised by individual respondent include- ❖ It should be made clear that the person to be examined (orally) must (a) be physically present at such an	❖ Our proposal does not change the present position that the person summoned for examination must (a) appear before the court and (b)

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	examination (i.e. he cannot just ask his legal team to attend on his behalf) and (b) provide the answer himself as opposed to by his solicitors / counsel (of course by reference to his legal team).	answer personally any question as the court may put to him or allow to be put to him at such examination.
	■ A respondent opined that the aim of section 221 of the C(WUMP)O is to summon the person to be examined on oath by the court as he should possess personal knowledge of the company. If he could employ solicitor/counsel to make representations on his behalf, the purpose of having such examination would be defeated and it may be a waste of time and costs for the solicitor/counsel to go back to the person to be examined to take instruction on the questions being asked.	■ Under the current proposal, an examinee must answer personally any question as the court may put to him or allow to be put to him. The solicitor or counsel to be employed by the examinee may only explain or qualify any answer given by the examinee personally or make representation (but not to answer a question) on behalf of the examinee.
21	***To provide that the documents and reasons submitted to the court by the applicant in support of his application under section 221 or section 222 of the C(WUMP)O should not be open for inspection by any person, except in so far as the court may order***	
	■ An overwhelming majority of respondents supported this technical proposal.	■ We will proceed to include the proposal in the draft legislation.
	■ Other comments raised by individual respondents include- ❖ This should be subject to judicial application.	❖ As the disclosure of the documents and the reasons in support of the application may adversely affect the effectiveness or even frustrate the purpose of examination (e.g. the targeted person may be alerted to conceal, dissipate or destroy information or material which may tend to incriminate himself but is relevant to the liquidator's investigation), the documents and reasons in support of the application should in general be kept confidential. Our proposal already provides that the court may on application allow the intended examinee to see all or part of the evidence in support of the application if the court is satisfied that it would be unfair to him if he is not allowed to see the evidence. There is a similar provision under the BO.

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	<u>Other general comments not specifically on the legislative proposals</u>	
1	■ Under the existing legislation, employees' outstanding entitlements owed by the company are accorded a lower priority in payment than the liquidator and the secured creditors and this undermines the employees' interests. A respondent suggested to accord the highest priority to outstanding wages owed to employees, so as to protect the employee's interests.	■ It should be noted that it is the basic principles of the corporate insolvency law of comparable common law jurisdictions (e.g. the UK, Australia and Singapore) that (a) the proprietary rights of a secured creditor over his security should generally not be interfered with by the liquidation process and that the security he has taken does not form part of the pool of assets for generating the fund for distribution amongst unsecured creditors; and (b) the liquidator's charges and liquidation expenses are generally payable out of the realised assets of the company in priority to other claims. In fact, under our existing legislation, employees are already accorded the highest priority amongst all unsecured creditors in relation to certain debts ahead of other preferential debts such as deposits in a bank winding-up and Government's statutory debts.
2	■ At present, after a company is wound up voluntarily, employee can only receive a maximum of $8,000 for outstanding wages and salary, $2,000 for wages in lieu of notice, and $8,000 for severance payment, as preferential payments. The preferential payments should be adjusted upwards to bring them in line with the Protection of Wages on Insolvency Fund ("PWIF") in order to protect employees' interests, Adjusting the aforesaid caps upward would help replenish the PWIF as the PWIF is entitled to a subrogated right.	■ It should be noted that any upward adjustment of the aforesaid caps in respect of employees' outstanding entitlements will affect the interests of other creditors by reducing the amount of realised assets available for distribution to them. A balanced view should be taken and it would not be appropriate to introduce any such change without considering the views of the other relevant stakeholders.
3	■ It should be provided in the legislation that when the company initiates a winding-up, in particular a voluntary winding-up, the company should inform its employees of the same in writing . Any contravention of this requirement should be made an offence.	■ If there are outstanding entitlements owed to the employees at the time of the winding up of the company, the employees will become creditors of the company. The C(WUMP)O provides that in a court winding-up, the petitioner of the winding-up is required to place advertisement in newspaper and gazette, and the winding-up order will also be gazetted.

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		In a voluntary winding-up, the company is required to gazette the resolution of winding-up within 14 days from the date of resolution. As regards creditors' voluntary winding-up, the liquidator is required to convene a creditors' meeting. Therefore, the present requirements already ensure employees will be informed of the matter at the same time with other creditors.
4	■ There is no such provision in Hong Kong to facilitate cross-border insolvency of foreign companies despite the fact that it is very common for businessmen in Hong Kong to use corporate vehicles incorporated in other jurisdictions to carry on their business. Foreign liquidators dealing with the assets located in Hong Kong have to apply for a winding-up order against the foreign companies under Hong Kong law which would be time consuming and, not cost effective, as all statutory obligations under C(WUMP)O have to be complied with and there is no power for the Court, let alone the liquidator, to dispense with compliance with such statutory obligations. The consultation document should have proposal on recognition of winding-up order and appointment of provisional liquidators or liquidators from certain jurisdictions. Many Hong Kong companies have set up branches in the mainland. These local companies may transfer their assets to their associated enterprises in the mainland before winding-up. The Government should be aware of the issues relating to these cross-border insolvency cases and implement suitable measures to handle this type of cases.	■ At present, the court has the power to deal with certain cross-border insolvency cases under section 327 of the C(WUMP)O. However, there are certain limits to the extent to which a Hong Kong court will recognise the vesting and discharging effects of a non-Hong Kong order. We note that while some overseas jurisdictions have adopted the Model Law on Cross-Border Insolvency of the United Nations Commission on International Trade Law, many jurisdictions, particularly those in Asia (e.g. Singapore and the Mainland), still rely on the local legislation to handle such cases. We will closely monitor the international development in this regard and will consider how best to take forward the matter.

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5	■ In light of the recent financial crises, and with an on-going trend by which more jurisdictions are considering to adopt corporate rescue practices, it is of high importance for the Government to re-approach the topic in order to align Hong Kong with other common law regions in the world and to bring up-to-date protections for businesses in financial difficulties.	■ The Government is now actively developing the proposal to introduce a new statutory corporate rescue procedure for Hong Kong. Since the last public consultation on the introduction of a corporate rescue procedure, the Government has been studying the various other key issues of the proposals. We are further consulting stakeholders on the detailed proposals in 2014.
6	■ In the UK, insolvency practitioners provide confirmation of debts for credit insurance claims purposes. This should be formally adopted under the proposed new Ordinance in Hong Kong and that confirmation is given direct to the credit insurer that the debt is duly acknowledged and accepted.	■ Currently, under rule 104 of the CWUR, a liquidator is required to, within 28 days after receiving a proof, either admit or reject the proof wholly or in part, or to require further evidence in support of it. If the creditor so wishes, he may transmit the liquidator's confirmation of a debt being admitted to an insurer for credit insurance purpose.
7	■ It would be unnecessary to rigidly stipulate that the provisional liquidator be appointed by the court in a voluntary winding-up, otherwise the operating cost would severely go up and it would be unaffordable for small and medium enterprises.	■ There is no proposal to stipulate that a provisional liquidator in a voluntary winding-up must be appointed by the court.
8	■ A liquidator is required under section 253 of the C(WUMP)O to publish a notice of his appointment or cessation of his appointment as liquidator by way of gazette containing the prescribed information including his name and also his identity card number or passport number. Consideration should be given if the publication of the liquidator's identity card or passport number is indeed necessary, and whether measures should be introduced to protect the personal data of liquidators. The personal data of individuals which have been published in the public domain may be put to secondary improper use by third parties.	■ The requirement for including the identity card number or passport number of the liquidator in a notice of appointment published in the Gazette pursuant to section 253(1) of the C(WUMP)O was formerly contained in Rule 46 of and Form 28 in the Appendix to the CWUR. Rule 46 and Form 28 have since been repealed by virtue of the Companies (Amendment) Ordinance 2003 (28 of 2003).

Item	Summary of Respondents' Views	Government's Responses
9	■ The current litigation funding regime, which is purely based on case law, should be codified in the statute and more clarity should be provided (e.g. procedures, priority in repayment of costs and the funder's position to share a portion of the recovery from the litigation). The clarity in this area will help to promote and encourage the creditor or other funder to provide funding or financial support to the liquidator in carrying out his duties.	■ There is a body of case law in the application of the litigation funding regime, and the benefit for codifying the common law position in the current legislation is not sufficiently clear.
10	■ Consideration should be given as to whether a liquidator is able to obtain a "catch all" global approval to compromise debts and utilise other powers available to him at the first meeting of creditors, as this may have significant cost savings for small liquidations and avoid the need to seek the COI or court approval on every matter, particularly in relation to debtors.	■ For certain powers the exercise of which requires prior sanction from either the COI or the court, there are clear benefits for requiring such sanction to be given on a case by case basis taking into account the prevailing circumstances. Not only is a "blanket" approval inadequate for dealing with changes and developments that evolve during the liquidation process, it also undermines the ability of the COI and the court to monitor the liquidation process on an on-going basis.
11	■ For court winding-ups where an insolvency practitioner other than the OR is appointed as the liquidator by court, security is required to be given by the appointed liquidator to the OR under the C(WUMP)O. In the circumstances, amendments to the C(WUMP)O and the corresponding CWUR are recommended such that (a) objective criteria should be set out in Rule 47 of the CWUR to facilitate the assessment of the form and value of the security required; (b) costs of security shall be payable out of the estate of the company in liquidation; (c) a "global bond" arrangement should operate for each firm of private insolvency practitioners as opposed to on a case-by-case basis.	■ (a) When fixing the amount and nature of security for individual cases, the OR would take into consideration the circumstances of each case. It may not be appropriate to exhaustively set out the criteria in the CWUR. (b) Under Rule 47 of the CWUR, a private insolvency practitioner acting as a liquidator in a court winding-up is required to give security to cover any default for which the liquidator is liable in relation to the administration of the winding up. Therefore, the cost of furnishing the security should be borne by the liquidator personally and shall not be charged against the assets. (c) While the security must be given as the OR directs, rule 47(b) of the CWUR provides that the security may be given either specifically in a particular winding-up, or generally to be available for any winding-up in which the person giving the security may be appointed.

Item	Summary of Respondents' Views	Government's Responses
12	■ Fee payable to the OR may be chargeable according to paragraph 1 of Table B of Schedule 3 to the Companies (Fees and Percentages) Order (Chapter 32C) under different heads of terms, charging either on fixed fee or according to a scale rate in proportion to the amount of "assets realised or brought to credit by the OR". However, the meaning of "assets realised or brought to credit by the OR" should be clarified to allow for greater clarity in its application.	■ It appears nothing inherently unclear in the definition of "assets realised or brought to credit by the OR" which requires clarification. We do not consider that there is a need to amend the existing legislation.
13	■ In practice, many directors are late or fail to submit the statement of affairs claiming that books of accounts are not up-to-date or information is not available. The statement of affairs, if submitted, is quite often incomplete and there is a lack of relevant information useful for the liquidator to pursue asset recovery and investigation. To improve this situation, heavy penalty should be imposed as a deterrent as the current penalty upon conviction to a level 5 fine and a daily continued default fine of HK$300 for non-compliance is rather low and does not achieve such warning purpose.	■ The maximum penalty level for non-compliance with the requirements for submission of a statement of affairs is already higher than the maximum penalty level for offences of a similar nature (e.g. section 300B(5) of the C(WUMP)O i.e. failure to submit a statement of affairs to a receiver).
14	■ Non-compliance with section 121 of the old CO (now sections 373, 374 and 377 of the new CO) and section 274 of the C(WUMP)O for not keeping proper books and records should be common for companies in liquidation. The law should be amended to include a presumption that directors for insolvent companies should be prime facie liable for such offence and the burden of proof rests with them to defend for his/her position. Besides, enforcement of the penalty of a fine of	■ Presuming a director being liable for an offence and requiring him to rebut the presumption is inconsistent with the common law principle of presumption of innocence as enshrined in Article 87 of the Basic Law and Article 11(1) of the Bill of Rights Ordinance (Chapter 383). The maximum penalty level for offences under section 121 of the old CO (now sections 373, 374 and 377 of the new CO) and section 274 of the C(WUMP)O is already at a relatively high level as compared with that for other offences in the new CO/C(WUMP)O. In appropriate cases where the conduct of a director warrants, the OR will apply to the court

Item	Summary of Respondents' Views	Government's Responses
	HK$300,000 and for 12 months imprisonment (see section 374 of new CO) should also be revisited. Upon conviction of the offence under sections 121 and 274, the directors should be disqualified for at least 5 years and it should be sanctioned by advertisement in public notices and the public search on disqualified directors should include information as to the offences committed, in particular on fraud.	for a disqualification order against the director. We have not received any feedback requesting for a review in this regard.
15	■ The threshold for taxation of bills or charges of solicitors, managers, accountants, auctioneers, brokers employed by the liquidator as provided under rule 179 of CWUR should be revised upward, say to HK$15,000, as it is not cost-effective and causes numerous administrative burden to tax bills at HK$3,000, given the fact that the current average hourly charge-out rate for a fee earner may be up to HK$3,000 or above.	■ To streamline the winding-up process, it is our proposal to allow the bills of costs or charges of the agents employed by the liquidator to be determined by agreement with the COI. The proposed alternative procedure would allow liquidators to deal with bills of agents in a more efficient manner without taxation, irrespective of the amount of the bill involved.

Detailed Proposals on a statutory Corporate Rescue Procedure ("CRP")

	Issues	Key Proposals
General Approach		
1	General approach	1.1 A Corporate Rescue Procedure ("CRP") is a legal framework which provides an option for a company in financial difficulty to seek to turn around and revive its business as much as possible, instead of proceeding with winding up immediately. The design of the CRP regime for Hong Kong should reflect the following important considerations - (a) The CRP should stipulate a defined timeframe for specified actions to facilitate speedy determination by creditors on the way forward for the company; (b) The CRP should provide that an independent third party, namely the provisional supervisor ("PS"), to take temporary control of the company. The PS would consider options for rescuing the company and prepare proposals for a voluntary arrangement; (c) The PS would be required to make recommendations on the specified alternative outcomes for the creditors' consideration and decision; (d) To enable the PS to focus on the formulation of the rescue plan, there should be a moratorium on legal actions and proceedings against the company when the company is under provisional supervision; (e) There should be appropriate checks-and-balances measures on the exercise of powers by the PS and the supervisor; (f) Employees of the company should be no worse off than in the case of an immediate insolvent winding-up; and (g) The CRP should involve predominantly out-of-court arrangements to save time and costs. 1.2 The detailed procedural and operational aspects (e.g. in respect of the proceedings at creditors' meetings and the formation of a committee of creditors) should as far as possible be modelled on the existing winding-up regime which our business sector and practitioners are familiar with.
Initiation of Provisional Supervision /Appointment of Provisional Supervisor		
2	Statutory objective of CRP	2.1 The objective of CRP is to maximise the chance of existence of the company or as much as possible its business, and if this is not attainable, to achieve a better return for the creditors of the company than in case of

	Issues	Key Proposals
		an immediate insolvent winding-up.
3	Insolvency being a pre-requisite for initiating CRP	3.1 Insolvency or likely insolvency should be a pre-requisite for commencing the CRP. The existing insolvency test used in the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) ("CWUMPO") would be adopted (i.e. a mixture of the cashflow and balance sheet tests).
4	Companies to which CRP may apply	4.1 The CRP should be applicable to local as well as overseas companies formed / registered under the Companies Ordinance (Cap. 622) ("CO") or a former Companies Ordinance (as defined in the CO), except for the following categories of financial institutions which are subject to regulation by statute that has provision for the relevant regulator to assume control of these financial institutions or oblige them to act in a certain manner, viz- (a) authorized institutions regulated by the HKMA under the Banking Ordinance (Cap. 155); (b) insurers regulated by the Insurance Authority under the Insurance Companies Ordinance (Cap. 41); (c) recognised clearing houses, recognised exchange companies, recognised exchange controllers, recognized investor compensation companies or licensed corporations; or persons authorised to provide automated trading services under the Securities and Futures Ordinance (Cap. 571); and (d) financial institutions not mentioned above but are to be subject to the proposed resolution regime.
5	Parties who may appoint PS for commencement of provisional supervision	5.1 The provisional supervision is commenced by the appointment of a PS. 5.2 The following parties may appoint a PS- (a) The company (either by a directors' ordinary resolution[1] or a members' ordinary resolution[2]), subject to the following conditions - (i) Must be of the opinion that the company is or is likely to become insolvent (See Item 7.1(c)). (ii) Must first obtain the written consent from the major secured creditor for initiation of the provisional supervision and for the appointment of the PS. (iii) The company resolves to appoint a PS at a meeting which must be held within 10 business days after

[1] This threshold is the same as that of initiating a voluntary winding-up under section 228A of the CWUMPO.

[2] This threshold is lower than that of initiating a company's voluntary winding-up. Section 228 of the CWUMPO provides that a company may be would up voluntarily by a special resolution of the members.

	Issues	Key Proposals
		the major secured creditor's written consent under sub-item (a)(ii) above has been sought. (b) Liquidator ("L") or Provisional Liquidator ("PL") in all forms of winding-up (i) If the L or PL is of the opinion that the company is or is likely to become insolvent, he may apply to the court for leave to appoint a PS, thus turning the winding-up to a provisional supervision. (ii) Prior written consent of the major secured creditor for initiation of the provisional supervision and for the appointment of the PS is also a pre-requisite. (iii) The application to court referred to in sub-item (b)(i) must be made within 10 business days after the major secured creditor's consent under sub-item (b)(ii) has been sought. (iv) After the leave of the court has been granted, the L or PL must appoint a PS within 10 business days. (v) The L / PL is eligible to be appointed as the PS of the company. *[Note: We will consider further whether, in case the company does not have a major secured creditor, prior consent from all secured creditors should be required before the company could initiate the CRP.]* 5.3 No person may be appointed as PS after the commencement of winding-up, unless the appointment is made by the L or PL.
6	Major secured creditor	6.1 A "major secured creditor" is defined as follows- (a) the holder of a charge, whether fixed or otherwise, over the whole or substantially the whole of the company's property; or (b) the holder of two or more charges, whether fixed or otherwise, on the company's property where the property subject to those charges constitutes the whole or substantially the whole of the company's property.) 6.2 By way of clarification, "major secured creditor" may include major secured creditors of successive charges of the company. 6.3 A "security" means any mortgage, charge, lien or other security.
7	Requirements in respect of the	7.1 The following requirements, which are similar to the proposed requirements for L/PL under the corporate insolvency law improvement exercise, would apply with respect to the appointment of PS -

	Issues	Key Proposals
	appointment of PS	(a) Certain types of persons would be disqualified for appointment as PS[3], including persons who are considered having a conflict of interest to act as a PS[4]. The appointment of a disqualified PS shall be void and the person concerned shall be subject to criminal liability. (b) PS would be required to prepare a declaration of relevant relationship to enhance transparency. He should also make a declaration of indemnity to let the creditors have the information that who has provided or would provide indemnity to the PS' work and decide on the potential conflict of interest it may have. The two declarations should be tabled at the 1st creditors' meeting for creditors' consideration before voting (See Item 29.3(d) below). (c) PS would need to provide consent in writing for his appointment. A list of prescribed information should be provided by the appointor in the notice of appointment, e.g. CRP is applicable to the company (See Item 4.1); the company is insolvent or likely insolvent (See Item 3.1); major secured creditor's consent for CRP has been obtained (See Item 5.2(a)(ii) and (b)(ii)), etc. 7.2 The appointment of PS takes effect immediately upon appointment.
8	Restriction on repeated CRP process	8.1 Unless the court approves otherwise on application by the company, a person may not be appointed by the company as PS of the company during 2 specified period: (a) if a voluntary arrangement takes effect following a provisional supervision – the period beginning with the date when the voluntary arrangement takes effect until the expiry of 12 months from the date the voluntary arrangement ceases to have effect; and (b) in any other cases – the period of 12 months beginning with the date immediately after the provisional supervision ends. 8.2 This time bar is not applicable to CRP cases initiated by L/PL who are required to obtain the leave of the court in appointing a PS.

[3] The types of disqualified persons will follow the proposals in the consultation on "Improvement of Corporate Insolvency Law"

[4] A creditor, debtor, director and former director, secretary and former secretary, auditor, or receiver or manager of the company.

	Issues	Key Proposals
Effect of Provisional Supervision and Rights of Secured Creditors		
9	Effect of provisional supervision on ongoing winding-up / receivership	9.1 Upon commencement of provisional supervision, subsisting winding-up proceedings would be suspended. 9.2 (a) Any receiver in office at the time when the company enters into provisional supervision may not perform or exercise a function or power as a receiver of that company when the company is under provisional supervision. (b) PS would have the right to take over the company's property held by the receiver and may request the receiver to vacate office.
10	Effect of provisional supervision on officers / members of company	10.1 PS would assume control of the company's property, business and affairs. The functions and powers of company officers would be suspended during the full period of provisional supervision except to the extent approved by the PS, whether or not at any particular time in that period there is a vacancy in the PS.
11	Effect of provisional supervision on property of the company	11.1 The appointment of a PS would not affect the title to the company's property. 11.2 A transaction dealing with the company's property after the commencement of the provisional supervision would be void unless it is entered into by PS or with a court order.
12	Effect of provisional supervision on contracts of the company	12.1 The appointment of PS alone does not automatically terminate contracts entered into by the company except that contractual ipso facto clauses would continue to be enforceable.
13	Effect of provisional supervision on limitation of action	13.1 The limitation period would be extended or deferred automatically according to the length of the period in which an action is prevented by the moratorium from being taken.
14	Setting-off by netting the obligations between creditors and	14.1 The moratorium set out in Item 15 below would not affect the right of set-off against the company. 14.2 Since both setting-off and the enforcement of ipso facto clauses would be allowed during the moratorium, it

	Issues	Key Proposals
	the company under provisional supervision	obviates the need to consider whether there should be specific exemption for some financial contracts and what sort of financial contracts should be exempted from the moratorium.
15	Moratorium on proceedings and other legal process during provisional supervision	15.1 When the company is in provisional supervision, the following moratorium will have effect- (a) Company cannot be wound up voluntarily (court winding-up is prohibited by virtue of the stay of all proceedings below); (b) Proceedings against the company or any of its property cannot be begun or proceeded with except with PS's written consent or the leave of court (except criminal proceedings or a prescribed proceeding); (c) No enforcement process on the company's property except with the leave of court; (d) Execution by a court officer cannot be taken except as permitted by court, and the court officer must deliver to the PS property of company in possession of the court officer, and pay to PS all proceeds from execution taken; and (e) Restriction on the exercise of third party property rights except with PS's written consent or the leave of court. 15.2 There will be exemption of the moratorium under the following circumstances- (a) If the company fails to pay the pre-commencement outstanding employees' entitlements according to the phased payment schedule (details in Item 35), the employees concerned will no longer be bound by the moratorium, e.g. they may petition to the court for winding-up the company; (b) Claims in respect of arrears of wages and other entitlements under the Employment Ordinance and outstanding employers' contributions to MPF or ORSO arising after the commencement of provisional supervision are exempted from the moratorium, e.g. they may petition to the court for winding-up the company; (c) Petition made under sections 723 to 727 of CO (unfair prejudice); or (d) Relevant proceedings or legal process in relation to the exercise of certain powers under the Securities and Futures Ordinance (to be confirmed with SFC).
Status, Role, Duty and Powers of Provisional Supervisor		
16	Joint and several appointment of PS	16.1 Two or more persons may be appointed to act jointly and severally as the PS.

	Issues	Key Proposals
		16.2 All persons appointed to act as PS are to perform the functions and exercise the powers of PS jointly and severally, unless otherwise stated in the relevant appointments which may specify which functions and powers (if any) are to be performed/exercised by any or all of the persons appointed. 16.3 Where a PS has already been appointed, another person may also be appointed to act as PS on the condition that - (a) the latter appointment is made by the original appointor; (b) consent to the latter appointment is given by the incumbent PS and the major secured creditor.
17	Removal and replacement of PS	17.1 Removal On application by the Official Receiver ("OR"), PL/L, the company or any creditor, the court may remove PS and appoint another one. 17.2 Filling vacancy (a) For vacancy in the office of PS (due to death, resignation, removal under Item 17.1 above, or ceasing to be qualified to act as PS[5] (See Item 7.1(a)), the original appointor may appoint another person as the replacement PS. (b) Prior written consent of the major secured creditor for the proposed replacement PS is also required before the appointment can be made. (c) Except where the replacement PS is appointed by the court under Item 17.1, the requirements vide Item 29 will apply, viz. the replacement PS so appointed must convene a creditors' meeting to consider whether to replace him; and as soon as practicable after his appointment, he must make declarations of relationships and indemnities and give the same to the creditors together with the notice calling the creditors' meeting. 17.3 Resignation (a) A PS who desires to resign his office shall summon a creditors' meeting to decide whether or not the resignation shall be accepted.

[5] Following the winding-up regime in Hong Kong and the improvement proposals, an undischarged bankrupt, a body corporate, mentally incapacitated persons, persons subject to a disqualification order of CWUMPO, and persons considered having conflict of interest are prohibited from being appointed as PS.

	Issues	Key Proposals
		(b) If the resignation is accepted, the PS shall give notice in writing to his appointor and to the company. (c) A PS has to file the notice of his resignation to the Registrar of Companies ("R of C"). (d) If the resignation is not accepted by the creditors' meeting, the PS may make an application to the court to determine whether the resignation shall be accepted.
18	Status and role of PS	18.1 The PS would act as an agent of the company in exercising his functions under the law.
19	Duties of PS	Duties of PS would include – 19.1 <u>Investigation and Recommendation of action</u> investigating company's business, property affairs and financial circumstances, and forming an opinion on each of the following matters - (a) whether it would be in the creditors' interests to implement a voluntary arrangement; (b) whether it would be in the creditors' interests to wind up the company; or (c) whether it would be in the creditors' interests to end the provisional supervision. 19.2 <u>Assumption of control</u> on his appointment, taking control of the company's business and affairs and taking custody and control of the property to which the company is or appears to be entitled. 19.3 <u>Lodging of reports</u> (a) lodging reports with the Official Receiver's Office and Companies Registry ("CR") if- (i) a past or present officer, employee or member of company may have been guilty of an offence in relation to the company, or (ii) a person who has taken part in the formation, promotion, administration, management or winding up of the company may have misapplied or retained, or has become liable or accountable for, money or property, or (iii) a person may have been guilty of negligence, default, breach of duty or breach of trust in relation to the company. (b) PS being held liable in case of non-compliance of the filing requirement 19.4 <u>Procedural duties</u> (a) calling of 1st and final creditors' meeting;

	Issues	Key Proposals
		(b) giving reports to creditors (for the purpose of the final creditors' meeting); (c) verifying employees' pre-commencement entitlements within 30 calendar days.
20	Powers of PS	20.1 The general powers of PS would include – (a) carrying on company's business and managing company's property and affairs; (b) terminating or disposing of part or all of company's business, and any of company's property; and (c) performing any function and exercising any power that the company or any officer could perform or exercise if the company were not under provisional supervision. 20.2 The PS has the following specific powers– (a) Remove a director of the company from office; (b) Appoint a person as a director of the company, whether to fill a vacancy or not; (c) Seek directions from the court; (d) Execute document, bring or defend proceedings, or do anything else in company's name and on its behalf; and (e) Whatever else necessary for the purpose of the provisional supervision
21	Powers to deal with charged / hire-purchase properties	21.1 PS would have the power to dispose of or take action relating to property which is subject to floating charge, as if it were not subject to the charge. The floating charge holder would then have the same priority in respect of the money acquired in exchange. *[Note: The nature of a floating charge is that the company is free to deal with the assets comprised in a floating charge in the ordinary course of its business until crystallization.]* 21.2 For non-floating charges, PS would have the power to apply to court to dispose of property subject to security (other than a floating charge) as if it were not subject to the security. The court may make such an order only if it thinks that the disposal would be likely to promote the purpose of the provisional supervision. If the proceeds of the disposal is not enough to cover the sums secured by the security, the net proceeds of disposal together with such amount of money necessary to make up the difference with the amount determined by the court would be applied towards discharging the sums secured by the security. 21.3 PS would have the power to apply to court to dispose of goods which are in the possession of the company

	Issues	Key Proposals
		under a hire-purchase agreement as if all the rights of the owner under the agreement were vested in the company. The court may make such an order only if it thinks that the disposal would be likely to promote the purpose of the provisional supervision. If the proceeds of the disposal is not enough to cover the sums payable under the hire-purchase agreement, the net proceeds of disposal together with such amount of money necessary to make up the difference with the amount determined by the court would be applied towards discharging the sums payable under the hire-purchase agreement.
22	Personal liabilities of PS and indemnity for debts of provisional supervision	22.1 <u>Personal Liabilities of PS</u> (a) PS would be personally liable for new contracts entered into him after his appointment (including employment contracts) (b) PS would also be personally liable for the pre-appointment contracts (including employment contracts) adopted by him in writing. PS would have 16 business days after the commencement of provisional supervision to decide whether to adopt the pre-appointment contracts. *[Note: Contracts would not be deemed to be adopted by the PS if he has not adopted them.]* 22.2 <u>Extent of personal liabilities</u> (a) PS would be held responsible for the contracts he had entered into as PS of the company. He would not be personally liable on contracts entered into by his predecessor(s). (b) However, the contracts entered into by his predecessor(s) will by nature be pre-appointment contracts for the current PS, and they would be open for him to adopt (See Item 22.1(b)). The current PS would become personally liable under such adopted contracts as from the adoption of the contracts, i.e. so far as the liabilities arise by reference to things done or occurred as from the adoption of the contracts. (c) The period in which the PS would be held liable is from the date of adoption / entering into of the contracts by the PS to the end of provisional supervision. 22.3 <u>Contracting-out of personal liabilities</u> PS would be allowed to agree with the concerned contracting parties on the extent of his personal liability. 22.4 <u>Indemnity for personal liabilities</u> PS would be entitled to be indemnified out of the company's property in his custody for debts he is personally liable (See Item 22.1), his remuneration and other expenses properly incurred by him, which is in turn secured by a

	Issues	Key Proposals
		lien over the company's property. The indemnity would have priority over all other claims e.g. floating chargees and unsecured creditors.
23	Protection of persons dealing with PS	23.1 Third party protection would be provided for a person 'dealing in good faith and for value' with PS e.g. when a person deals with a PS during provisional supervision, the company will still be bound by the dealing if the person has acted 'in good faith and for good consideration' for that dealing.
24	Qualification of PS	24.1 Persons having the following qualifications will be eligible to take up appointment as PS- (a) Certified public accountants; or (b) Solicitors with practicing certificates 24.2 HKICPA and the Law Society of Hong Kong would take up the role of regulators regulating practitioners within their own membership in accordance with their professional requirements respectively.
25	Remuneration of PS and the agents appointed by the PS	25.1 Remuneration of PS should be fixed by- (a) agreement between PS and committee of creditors (if any); (b) resolution of creditors; or (c) the court (failing the above). 25.2 Remuneration of the agents employed by the PS to assist in his work will form part of the expenses incurred by the PS (See Item 36.1(b)).
26	Action against PS	26.1 Challenge against conduct of PS (a) Any creditor or member may apply to the court claiming PS - (i) has managed the company's business, affairs or property in such a way that is prejudicial to the interests of some or all of the company's creditors or members; or (ii) has done an act or made an omission, or proposes to do so, that is or would be prejudicial to such interests. (b) The court may make such order as it thinks fit. 26.2 Misfeasance action (a) On application by OR, PS (to take action against the former PS), L, any creditor or member of the

	Issues	Key Proposals
		company, the court may examine the conduct of a person who has been a PS for the following - (i) PS' misapplication or retention of company's money or other property; (ii) PS' becoming accountable for company's money or other property; (iii) Breach of PS' fiduciary or other duty in relation to the company; or (iv) PS being guilty of misfeasance. (b) The court may order the person to repay, restore or account for money or property; pay interest; or contribute a sum to the company's property by way of compensation for breach of duty or misfeasance.
<u>Process and Termination of the Provisional Supervision</u>		
27	Notification and advertisement of PS's appointment	27.1 The requirements on notification and advertisement of appointment of PS are as follows - (a) <u>Gazette</u> PS should arrange for the notice of his appointment to be published in the Gazette at the first available gazette date after the latter's appointment. (b) <u>Newspaper advertisement</u> PS should arrange for the notice of appointment to be published in two local newspapers on the next business day following his appointment. (c) <u>Filing</u> PS should file the notice of appointment with CR on or before the next business day following his appointment. 27.2 The PS commits an offence if he fails to comply with any of these notification and advertisement requirements.
28	Publicity requirements	28.1 Publicity requirements during the period of provisional supervision are as follows - (a) to require stating in the company's documents that the company was "in provisional supervision"; (b) to provide that notification of the company was "in provisional supervision" had to be made in the company's website (if the company has a website). 28.2 (a) The company would commit an offence for non-compliance; and (b) Any officer of the company (i.e. includes a director, manager or company secretary of a company as defined under the CO) and the PS of the company would commit an offence if he knowingly and

	Issues	Key Proposals
		wilfully authorizes or permits the non-compliance.
29	First creditors' meeting	29.1 After the commencement of provisional supervision, there shall be a first creditors' meeting. 29.2 PS would be required to call the first creditors' meeting to decide on the following - (a) whether the PS (if more than one, any of them) should be replaced, and if so, to decide on the replacement PS; and (b) whether to appoint a committee of creditors, and if so, its members. 29.3 The procedures of calling the first creditors' meeting are as follows- (a) PS should give written notice to every person appearing in the company's book to be a creditor and as many of the company's creditors as reasonably practicable. (b) The meeting must be held within 10 business days from the date when provisional supervision commences. (c) There is a minimum 7-day notice period for convening the meeting, and the notice / the content of the notice should be prescribed in law. (d) PS would be required to prepare a declaration of relevant relationship and should also make a declaration of indemnity to be tabled at the 1st creditors' meeting for creditors' consideration before voting (See Item 7.1(b)). 29.4 In case the PS is replaced at the first creditors' meeting, the newly appointed PS is required to comply with the notification and advertisement requirements on his appointment (see Item 28). 29.5 PS (referred to in Item 29.2) should be liable to an offence for non-compliance with the requirements on calling the first creditors' meeting.
30	Committee of creditors	30.1 The first creditors' meeting will decide on whether to appoint a committee of creditors ("CoC"), and if so, its members (See Item 29.2(b)). 30.2 Functions of CoC are- (a) to be consulted any matters relating to the provisional supervision; and (b) to receive and consider reports by PS on the business of the provisional supervision.

	Issues	Key Proposals
31	Statement of company's affairs, gathering information and investigation of company affairs	31.1 Director and secretary of the company are required to submit a statement of affairs (SOA) to the PS within 28 days of the commencement of the provisional supervision. Non-compliance will attract criminal liability. 31.2 The PS may request certain persons (e.g. present/former officers and employees of the company as well as persons who took part in the company's formation within 1 year before the commencement of provisional supervision – the list of persons to be provided for in legislation) to give a SOA to him, and such persons shall do so within 28 days from receipt of the request. Non-compliance with the request will attract criminal liability. 31.3 The PS may also request certain persons (same as in Item 31.1 above) - (a) to deliver up to him the books and papers of the company in their hands; (b) to tell him the whereabouts of other books and papers of the company; (c) to attend on the PS and answer questions put to him, and give further information required by the PS; and (d) to give him such information about the company as required by him. Non-compliance with the request will attract criminal liability. 31.4 PS may apply to the court for examination of – (a) any officer of the company; (b) any person known or suspected by the PS to have in his possession any property of the company or indebted to that company; and (a) any person that the court thinks capable of giving information concerning the promotion, dealings, affairs etc. of the company.
32	Final creditors' meeting & specified outcomes of the meeting	32.1 After the first creditors' meeting was held, there shall be a final creditors' meeting when the company is under provisional supervision. 32.2 PS is required to call the final creditors' meeting. Upon having the PS' recommendation on the priority of the following specified outcomes (See Item 19.1), the final creditors' meeting will vote in the order of the PS' recommended priority to decide on one of the following specified outcomes for the company -

	Issues	Key Proposals
		(a) approval of a proposed voluntary arrangement for the company with or without modification (see Item 37); or (b) winding-up of the company; or (c) termination of the provisional supervision, for the company to revert to its pre-CRP status. 32.3 The procedures of calling the final creditors' meeting are as follows- (a) PS should give written notice to every person appearing in the company's book to be a creditor and as many of the company's creditors as reasonably practicable. (b) The notice of meeting should set out the date, time, and venue of the meeting, purpose for the meeting, matters like proxy and entitlement to vote, etc. and should be accompanied with the statement of affairs of the company (or summary), report of the PS, etc. (c) PS should summon the final creditors' meeting by not less than 7 days' notice of the time and place in the Gazette and in one or more local newspapers. (d) The final creditors' meeting must be held within 45 business days from the commencement of provisional supervision ("the time limit for holding the final creditors' meeting), subject to Item 33. (e) PS is required to prepare, and accompany with the notice of the final creditors' meeting to be given to the creditors, the following - (i) A report on the company's business, property, financial circumstances; (ii) A statement of the PS's opinion about each of the three specified outcomes (See Item 32.2); (iii) His reasons for those opinions; (iv) Such other information known to the PS as will enable the creditors to make an informed decision about each matter mentioned in (ii) above; (v) The result of the investigation by the PS of the company on any possible claims that may be taken by the L of the company (if the company were wound up by way of a creditors' voluntary winding-up on the commencement of provisional supervision) under the provisions on voidable transactions ; and (vi) A proposed voluntary arrangement achieving the purpose stated in Item 2 (if the PS proposes to pursue the specified outcome set out in Item 32.2(a)). 32.4 <u>Proceedings</u> The proceedings of the final creditors' meeting will be consistent with those for creditors' meeting in a winding-up under the existing CWUMPO e.g.- (a) A quorum of 3 creditors is required. If the number of creditors entitled to vote does not exceed 3, all the

	Issues	Key Proposals
		creditors are required for achieving the quorum. (b) If a quorum is not met within 30 minutes of the scheduled start of the meeting, the meeting would be adjourned automatically. (c) PS himself or a person nominated by the PS shall be the chairman of the meeting. 32.5 <u>Voting</u> (a) For passing a resolution to approve or modify a voluntary arrangement, the resolution would be passed if- (i) a majority of the creditors present and voting have voted in favour; and (ii) those voting in favour hold more than $66^{2}/_{3}$% of the total value of the creditors voting; and (iii) no more than 50% in value of those creditors who are not connected with the company[6] have voted against it. (b) For passing any other resolution, the resolution would be passed if- (i) a majority of the creditors present and voting have voted in favour; and (ii) those voting in favour hold more than 50% of the total value of the creditors voting; and (iii) no more than 50% in value of those creditors who are not connected with the company have voted against it. (c) Unless he surrenders his security, a secured creditor shall be entitled to vote only in respect of the balance (if any) due to him after deducting the value of his security. (d) Voting by proxy is allowed pursuant to the procedures to be prescribed for creditors' meetings. *[Note: A voting mechanism encompassing Items 32.5(a)(i) and 32.5(b)(i) would render the arrangement more in line with the similar requirement for passing an arrangement or compromise proposed to be entered into with the creditors under sections 673 and 674 of the CO.]* 32.6 <u>Adjournment</u> (a) Adjournment of the final creditors' meeting would be allowed to cover certain eventualities, for instance,

[6] The definition of "a person connected with the company" shall make reference to that in legislative proposal of the corporate insolvency law improvement exercise.

	Issues	Key Proposals
		quorum not met within 30 minutes of the scheduled start of the meeting. (b) The chairman of the meeting may (or must, if the meeting so resolved) adjourn the meeting, but the period of adjournment or total periods of adjournment must not exceed 14 calendar days from the date on which such meeting was originally held. That is, in any case, the final creditors' meeting must be held within a definite period of time. 32.7 PS should be liable to an offence for non-compliance with the requirements on calling the final creditors' meeting.
33	Extension of provisional supervision	33.1 A provisional supervision normally ends upon having a definite specified outcome resolved at the final creditor's meeting (See Item 34.2). Nevertheless, the time limit for holding the final creditors' meeting can be extended with the approval by the creditors at a meeting of creditors, provided that they may not approve such period or periods which would extend beyond the end of six months from the commencement of provisional supervision. 33.2 Extension of the time limit for holding the final creditors' meeting can also be granted by the court upon application made by the PS (whether the extension sought is within or beyond the end of six months from the commencement of provisional supervision). The court may grant an extension for a period as it thinks fit.
34	End of provisional supervision	34.1 Provisional supervision ends on the happening of whichever event referred to in Items 34.2 and 34.3 below happens first after the commencement of provisional supervision. 34.2 The normal outcome of the provisional supervision is that one of the following is resolved at the final creditors' meeting - (a) approval of a proposed voluntary arrangement; (b) winding-up of the company; or (c) termination of the provisional supervision, for the company to revert to its pre-CRP status. 34.3 However, provisional supervision will also end if any of the following arises - (a) the court orders that the provisional supervision is to end; (b) the final creditors' meeting is not held- (i) within the time limit for holding the final creditors' meeting (i.e. 45 business days from

	Issues	Key Proposals
		commencement of CRP, (See Item 32.3(d), subject to any duly approved extension (See Item 33)); and (ii) no creditors' meeting is convened for approving an extension of the time limit for holding the final creditors' meeting and no application is made to court for such extension; (c) where a creditors' meeting for extending the time limit for holding the final creditors' meeting is held but the extension is not approved, or where an application is made to the court for such extension, but the court did not order the extension; or (d) the final creditors' meeting ends (whether or not it was earlier adjourned) without a resolution being passed on the three specified outcomes set out in Item 34.2; or[7] (e) the court appoints a PL or orders that the company be wound up[8].
35	Pre-commencement employees' entitlements	A phased payment schedule will be provided for outstanding pre-commencement employees' entitlements as follows – 35.1 Arrears of wages before the commencement of the provisional supervision should be paid up to the Protection of Wages on Insolvency Fund ("PWIF")-cap by the 30th calendar day after commencement of the provisional supervision (1st phased payment). 35.2 For employees whose employment has been terminated before commencement of the provisional supervision, any outstanding wages in lieu of notice of termination, severance payments, pay for untaken annual leave and untaken statutory holidays[9] should be paid up to the relevant PWIF-caps (2nd phased payment) - (a) within 45 calendar days after the voluntary arrangement has been approved; or (b) if the time limit for holding final creditors' meeting is extended, within 45 calendar days from the date of the approval of the extension;

[7] Under Item 34.3(b) to (d), the company will revert to the pre-CRP status when the provisional supervision ends, whereas the court under Item 34.3(a) may make any relevant order as it thinks fit depending on the circumstances of the case.

[8] The circumstances where Item 34.3(e) may arise in case, for example, application is made to the court claiming that the PS has managed the company's business, affairs or property in a way prejudicial to the interests of some or all of the creditors or members (See Item 26.1) or the PS has failed to comply with the payment schedule in paying the pre-commencement outstanding employee's entitlements (See Item 35).

[9] The untaken annual leave and the untaken statutory holidays, which were not yet introduced into the law at the time of the 2010 consultation conclusions, were not included in the 2010 proposal. It is noted that after the last consultation exercise in 2009-10 and since June 2012, ex-gratia payments of PWIF have been extended to cover not only outstanding wages in lieu of notice of termination and severance payments, but also (i) pay for untaken annual leave and (ii) untaken statutory holidays.

	Issues	Key Proposals
		35.3 Any remaining pre-commencement entitlements, including outstanding employers' contributions under the Mandatory Provident Fund Schemes Ordinance (Cap. 485) or the Occupational Retirement Schemes Ordinance (Cap. 426), should be paid in full within 12 months after the voluntary arrangement has come into effect (3rd phased payment). 35.4 In relation to the pre-commencement employees' claims covered by the above phased payment schedule, the employees would be bound by the moratorium. If the phased payment schedule is not adhered to, any of the employees concerned would no longer be bound by the moratorium, e.g. they may petition to the court for winding up the company (thus eligible to apply for PWIF ex-gratia payments).
36	Priority of payments	36.1 The following payments will be accorded priority to all other payments (e.g. floating charges and unsecured debts)- (a) PS's personally liable debts (including the obligations under the new and adopted pre-appointment contracts) (See Item 22.1); (b) Expenses properly incurred by PS; and (c) PS's remuneration.
Process and Termination of the Voluntary Arrangement		
37	Detailed Procedure of the Voluntary Arrangement ("VA")	37.1 If the PS proposes a VA to the creditors at the final creditors' meeting, the following procedure will apply - (a) It is the duty of PS to prepare a proposed VA to be considered by the creditors at the final creditors' meeting. (b) The creditors may pass a resolution to approve the proposed VA, to approve the proposed VA with modifications, or to reject it. (c) If a resolution is passed to approve the proposed VA, the PS will be the supervisor ("S") of the VA, unless the creditors appoint another person to be S. (d) The terms of the VA would be contained in the resolution approved at the final creditors' meeting and the proposed VA prepared by the PS for the meeting, with any modification as approved at the meeting. (e) The S is required to file a notice with CR that the final creditors' meeting has approved a VA, with a copy of the approved VA (contained in the resolution and proposed VA as aforesaid). (f) S is required to send to each creditor a written notice of the approval of the VA. Gazette or newspaper

	Issues	Key Proposals
		advertisement is not required. 37.2 Publicity requirements during the period of VA are as follows – (a) to require stating in the company's documents that the company is "subject to Voluntary Arrangement"), and (b) to provide that notification of the company was "subject to Voluntary Arrangement" had to be made in the company's website (if the company has a website). (c) The company would commit an offence for non-compliance of sub-items (a) and (b); and any officer of the company and the S of the company would commit an offence if he knowingly and wilfully authorizes or permits the non-compliance.
38	Content of the VA of the company	38.1 The proposed VA should include but not limited to the following items – (a) The S; (b) The property of the company to be available to pay creditors' claims; (c) Powers and liabilities of S; (d) Conditions (if any) for the commencement of VA, conditions (if any) for the continuance of VA, and circumstances for termination of VA; (e) Moratorium terms (subject to statutory provisions mentioned in Item 40 below); (f) Formation of committee of creditors; (g) Phased payment of outstanding pre-commencement employees' entitlements; (h) To what extent the company is to be released from its debts; (i) The order in which proceeds of realizing the property in sub-item (b) are to be distributed among creditors bound by the VA; and (j) The day (not later that the commencement of provisional supervision) on or before which claims must have arisen if they are to be admissible under the VA 38.2 The proposed VA may also contain any other "optional" content. 38.3 The VA must not provide for any action which affects the right of a secured creditor to enforce his security except with the written consent of the relevant secured creditor.
39	Parties to be bound by the VA	39.1 The VA would bind the company, its officers and members and the S, and all creditors on claims arising on or before the day specified for such purpose in the VA.

	Issues	Key Proposals
		39.2 The provision in Item 39.1 does not prevent a secured creditor from exercising his right to enforce his security during the implementation of the VA except to the extent his right is affected by anything provided in the VA with his written consent.
40	Moratorium under the VA	40.1 Until the VA terminates, the following moratorium provisions apply to a person bound by VA - (a) no petition may be presented to the court to wind up the company and no petition presented previously may be proceeded with; (b) no resolution may be passed by the members or directors of the company for the winding-up of the company; (c) no proceeding against the company or in relation to any of its property may be begun or proceeded with, except with the leave of court; and (d) no enforcement process may be begun or proceeded with in relation to property of the company, except with the leave of court. 40.2 Any other additional moratorium provisions may be laid down in the VA, and the specific content are to be agreed by the creditors at the final creditors' meeting on a case-by-case basis.
41	Variation of the VA	41.1 Only S will be allowed to initiate the procedure to vary the VA, and S may do so by convening a meeting of creditors to consider whether to approve the proposed variation by a resolution passed in the creditors' meeting (procedures should follow those in Item 37). 41.2 On an application by a creditor made within 28 days from the approval of the variation on the ground that there was material irregularity at or in relation to the creditors' meeting approving the variation, the court may cancel or confirm, in whole or in part, the variation approved by the procedure in Item 41.1 above.
42	Termination of the VA	42.1 The VA is terminated upon the first occurrence of any of the following events - (a) the court orders the termination – (i) on an application by any creditor or the S within the period of 28 days after the final creditors' meeting which resolved to approve the VA, on the ground that there was material irregularity at or in relation to the final creditors' meeting; or (ii) on an application by a creditor of the company on the ground that the terms of the VA unfairly prejudices his interests; or

	Issues	Key Proposals
		(iii) on an application by any creditor or the S on the ground that the purpose of VA cannot be achieved or any other reason e.g. the circumstance(s) for termination as specified in the termination clause in the VA occurred; (b) a creditors' meeting resolves to terminate the VA; or (c) S executes a notice of termination after the final completion of the VA.
43	S	43.1 Powers and Duties (a) S shall have the powers and duties as provided in the VA; (b) The S of the VA may seek directions from the court; and (c) The S may apply to the court for conducting examinations of company officers or others who are or have been involved in the examinable affairs of the company. 43.2 Duty to send report (a) The S must keep accounts and records of his acts and dealings in, and in connection with, the VA, including in particular records of all receipts and payments of money. (b) The S must in respect of each 6-month period ending with the commencement of the VA send within 1 month a report on the progress and prospects for the full implementation of the VA to the company, all those creditors who are bound by the VA, members of the company, the company's auditors (if any) for the time being and R of C (for filing). (c) Not more than 1 month after the final completion or termination of the VA, the S shall send to creditors and members of the company a notice that the VA has been fully implemented or has been terminated. A copy of a report prepared by the S summarizing all receipts and payments made by him in pursuance of the VA should accompany the notice. The S shall also within the said 1 month file the notice with CR. 43.3 Qualifications The qualifications of S should be the same as for PS (See Item 24). 43.4 Disqualification Certain types of persons would be disqualified for appointment as S[10], including persons who are considered

[10] The types of disqualified persons will follow the proposals in the consultation on "Improvement of Corporate Insolvency Law"

	Issues	Key Proposals
		having a conflict of interest to act as a S[11]. The appointment of a disqualified S shall be void and the S shall be subject to criminal liability. 43.5 <u>Removal, resignation and filling vacancy</u> (a) On the application by OR or any creditor, the court may remove the S and appoint another one. (b) The S may resign by giving notice in writing to the company, subject to the agreement by a resolution at a creditors' meeting. (c) Where there is a vacancy in office of the S (due to death, ceasing to be qualified, removal under sub-item (a) or resignation), or where for some reason no S is acting, the court may, on application by OR, an officer, creditor or member of the company, appoint another one. 43.6 <u>Remuneration of S</u> Remuneration of S should be fixed by- (a) agreement between S and committee of creditors (if any); (b) (failing the above) resolution of creditors; or (c) (failing the above) the court. 43.7 <u>Remuneration of the agents employed by the S</u> This should be dealt with or provided for in the proposed VA to be voted on at the final creditors' meeting. 43.8 <u>Appointment of 2 or more S</u> (a) 2 or more persons may be appointed as the S. (b) Where 2 or more persons are appointed as S, a function or power of S may be performed or exercised by them jointly or severally, except so far as the VA or the resolution or instrument appointing them otherwise provides.
44	Action against the S	44.1 The provisions regarding action against S are to be the same as of PS (See Item 26).
45	Transition to creditors' voluntary winding-up	45.1 A company subject to provisional supervision or VA will become subject to a CVL - (a) where the creditors resolve at the final creditors' meeting that the company be wound up (See Item

[11] A creditor, debtor, director and former director, secretary and former secretary, auditor, or receiver or manager of the company.

	Issues	Key Proposals
	("CVL")	34.2(b)); (b) where the company is subject to VA, the creditors resolve, at a meeting convened by the S, to terminate the VA and also resolve at that meeting that the company be wound up (See Item 42.1(b)); or (c) if the court makes an order to terminate the VA and wind up the company (See Item 42.1(a)).
46	L of the deemed CVL	46.1 As the company may proceed to a CVL under Item 45.1(c) above without any creditors' meeting, it is necessary to deem the S of the VA as the L of the CVL at that stage, and this deemed L shall call a creditors' meeting to consider whether to appoint another L and a committee of inspection ("COI"). 46.2 (a) Under the scenarios of Item 45.1(a) and (b) where the creditors' meeting was held, the creditors at that meeting shall also consider whether to appoint an L and a COI. (b) If the creditors do not appoint a different person as the L by the end of the meeting, the creditors are taken to have appointed the S of the VA as the L of the CVL.
47	Publishing notice when a provisional supervision / supervision transits to a CVL	47.1 In any case where a company in provisional supervision or subject to VA is deemed to become subject to a CVL, the L shall within 14 days after the day on which the company is deemed to become subject to a CVL, give notice of such fact by publication of a notice in the Gazette.

Financial Services and the Treasury Bureau
Official Receiver's Office
28 May 2014

Detailed Proposals on Insolvent Trading Provisions

Annex C

	Issues	**Key Proposals**
1	Purpose	1.1 In order to encourage directors to act on insolvency earlier rather than later and to protect the interests of creditors dealing with a company, the liquidator of a company will be empowered to make an application to the court to seek a declaration that the director is civilly liable for insolvent trading and to make the director personally liable to pay compensation to the company which traded while insolvent. 1.2 Introducing insolvent trading provisions may facilitate the liquidator to obtain more assets of the company for the benefit of distribution to the unsecured creditors in a winding-up.
2	Insolvency as a key element for applying the insolvent trading provisions and the test for insolvency	2.1 Insolvency of the company is one of the key elements for applying the insolvent trading provisions. The existing insolvency test used in section 178 of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32) ("CWUMPO") would be adopted (i.e. a mixture of the cashflow and balance sheet tests).
3	Application of insolvent trading provisions	3.1 The insolvent trading provisions should apply to – (a) companies formed and registered under the Companies Ordinance (Chapter 622) ("CO") and the existing companies (i.e. those formed and registered under the former Companies Ordinances)[1]; and (b) 'unregistered companies' within the meaning of Part X of CWUMPO, other than a partnership or an association, (i) wherever incorporated, (ii) carrying on or have carried on business in HK, and (iii) capable of being wound up under CWUMPO. 3.2 The insolvent trading provisions should apply to 'persons' being – (a) directors as defined in section 2 of the CO; and

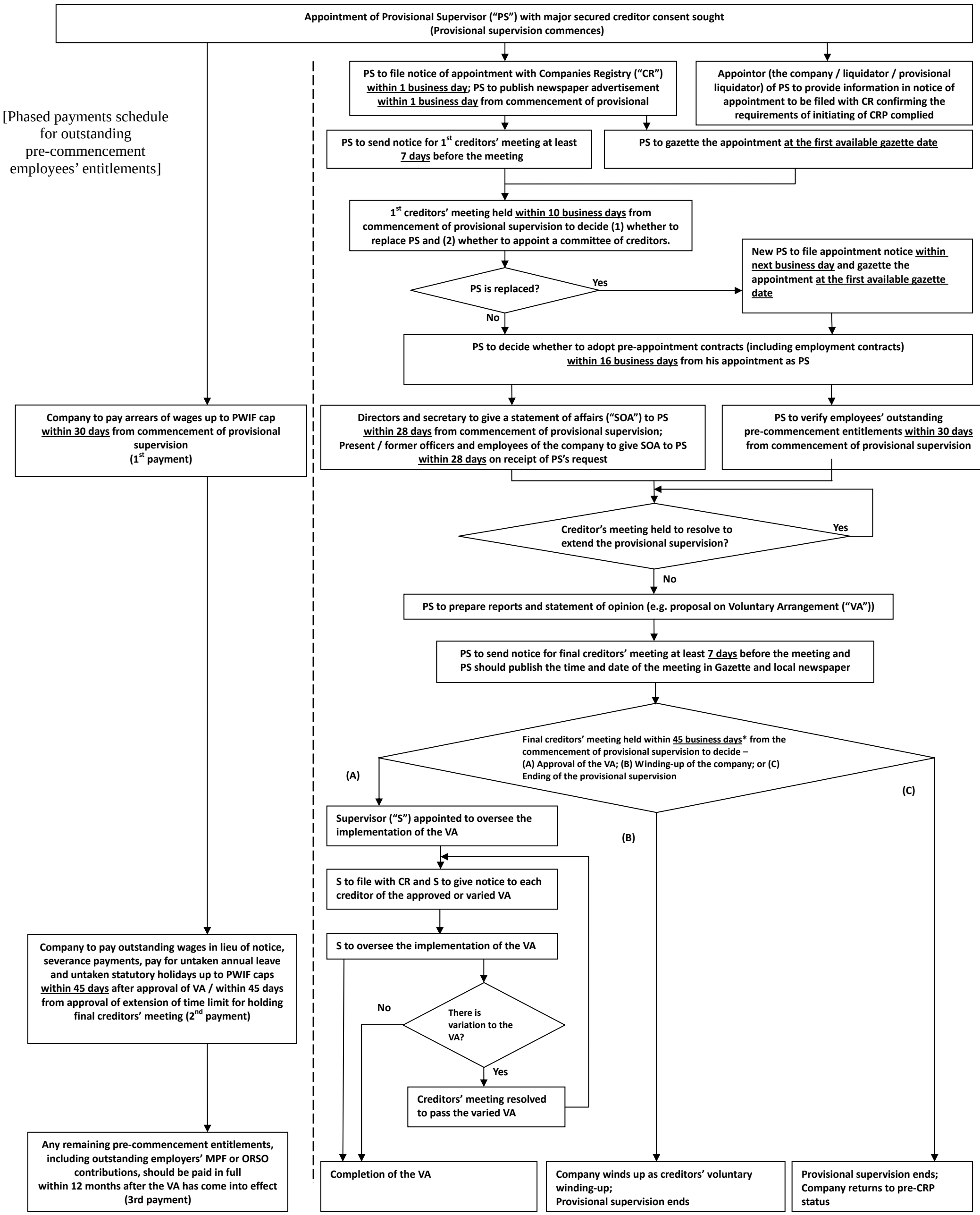
[1] This is the definition for a "company" within the meaning of section 2 of CWUMPO.

	Issues	Key Proposals
		(b) shadow directors as defined in section 2 of the CO.
4	Eligible applicant for applying to the court for invoking the insolvent trading provisions	4.1 Since the insolvent trading provisions will only apply when the company has gone into insolvent winding-up, the power to make an application should vest with the liquidator.
5	The constituents of liability	5.1 The following requirements must be satisfied before the court makes a declaration of insolvent trading – (a) A debt is incurred by the company; (b) The person is a director/shadow director of the company at the time the company incurs the debt; (c) The company is insolvent at that time or becomes insolvent by incurring that debt, or debts including that debt; (d) The director failed to prevent the company from incurring the debt; and (e) The director knew or ought to have known that the company was insolvent at that time or would become insolvent by incurring that debt or debts including that debt. 5.2 In determining whether the director has the constructive knowledge under Item 5.1(e) (i.e. he "ought to have known") and for assessing whether the defence(s) in Item 6 below has/have been established, the same test used in section 465 of the CO (regarding directors' duty of care, skill and diligence) will apply, as follows – (a) The facts which a director ought to know or ascertain, the conclusions which he ought to reach and the steps which he ought to take are those which would be known or ascertained, or reached or taken, by a reasonably diligent person having both— (i) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as are carried out by that director in relation to the company, and (ii) the general knowledge, skill and experience that that director has. 5.3 The provision has no retrospective effect i.e. insolvent trading transactions prior to the commencement of the law will not be caught.
6	Defence	6.1 It is a statutory defence if :- (a) the director has taken all reasonable steps to prevent the company from incurring the debt;

	Issues	Key Proposals
		(b) the incurring of the debt is part and parcel of the steps taken by the director concerned to initiate the corporate rescue procedure ("CRP"). *[Note: As regards Item 6.1(b), consideration will be given whether the scope of the proposed defence should be expanded to cover also an "arrangement or compromise" under the CO or an informal workout.]*
7	Type of order and nature of liability	7.1 Where the court makes a declaration of insolvent trading in respect of a director, it may order the person to pay such compensation to the company as the court thinks fit. 7.2 Only a civil liability is imposed on the director who is in contravention of the insolvent trading provisions.
8	Application of compensation	8.1 The insolvent trading application is made by the liquidator and the compensation from the application will be paid to the unsecured creditors. The compensation will not form part of the company's assets which could be caught by and be subject to any prior security interest granted by the company over the present and future assets of the company.

Financial Services and the Treasury Bureau
Official Receiver's Office
28 May 2014

Corporate Rescue Procedure ("CRP") FLOWCHART



*** The time limit for holding the final creditors' meeting can be extended with the approval by the creditors up to six months from the commencement of provisional supervision. The court may grant an extension for such period as it thinks fit.**